The Institute of Cost Accountants of India

(Statutory body under an Act of Parliament)

CMA e-Magazine

Cost Competitiveness

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Vision

CMAs would be the preferred source of resources and professionals for the Financial Leadership of enterprises globally.

Mission

CMA professionals would ethically drive enterprises globally by creating value to stakeholders in the regulatory context through competencies drawn from the integration of strategy, management and accounting acquired through focused training and continuous education.

THE INSTITUTE OF COST ACCOUNTANTS OF INDIA

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Editorial

A well-managed business is absolutely fanatic about continuous improvement; i.e., doing things better, faster, and cheaper. Customer demands, competitive pressures, and world economics force us to do things better, faster, and cheaper. The global business environment is characterized by intense competition from domestic players and multinational companies. Thus, formulating the right strategy is inevitable in order to establish competitive advantage.

In the recent past, the country has experienced suffering of public interest due to weak corporate governance, adversely affecting trust and confidence of investors and stakeholders. The Indian economy has to migrate from the current status to the top end position of the global competitiveness index in a short/ medium time span. Considering the maturity levels of cost and management accounting in Indian economy caused by the legacy of protected environment, we have a long way to traverse without luxury of time.

Cost Management and Cost Assurance leads to improvement of the productivity of all the resources, resulting in optimum utilization of resources and minimization of wastages. Cost information plays a critical role in transfer pricing, predatory pricing, fixation of margin of dumping for the purpose of levying anti-dumping duty, free trade agreement, consumer protection, revival of sick companies and corporate governance. Costing system is required for strategic planning and decision making as it provides timely warning signals thus enabling management to take appropriate decisions for sustained growth. Cost information is vital for providing the necessary inputs for making various Government plans so that the productivity and efficiency of resource utilization is kept in focus. Maintenance of proper cost records is also essential for fulfilling the objectives laid down under National Voluntary Guidelines (NVG) for economic, environmental and social responsibilities of business as the information provided by the cost records is compatible with the information requirements under NVG.

Since this is a blazing issue at present, the organizations are focusing on Cost Competitiveness for their sustainability. It is an attempt of our Directorate as a step to improve cost effectiveness. We look forward to constructive feedback from our readers for overall development of this e-Magazine. Please send your mails at *research@icmai.in*. We thank all the contributors to this important issue and hope our readers enjoy the articles.

Foreword

It gives me a distinct honour to present before you the ***e-Magazine*** of the Institute on ***"Cost Competitiveness"***. I believe that a glance through the pages of this bulletin will definitely enrich the knowledge base of the readers.

The role and importance of Cost and Management Accountants has increased manifold on account of growing competition in the corporate sector. The CMAs with expertise understanding and knowledge of the enterprise cost management systems can play a key role in leading light to the economic recovery process in the Indian Economy by efficiency, productivity, sustainability and competitiveness of industry. The Cost Accountants facilitate the management in regulating production operations and go ahead of processes of production. As Cost and Management Accounting deals with the cost and benefit analysis of a product or service, it demands analytical and attentive mindset with an objective outlook.

Cost Competitiveness is that level of operation which allows an organization to go on winning sales at a price that generates a sufficient level of return both for stakeholders and for the investment needs of the business. An effective Cost Competitiveness drives focus on eliminating wastage, shortcoming, addressing both the input and output. It lays the foundation for ongoing improvement by putting policies and control in place that prevents a reversion to old, unproductive practices. So in brief we can say competitiveness is the ability of a country's enterprises to sustain superior market positions and profitability relative to their domestic and international competitors.

The idea of innovation is the idea of progress. This edition covers a few interviews, case studies and innovative ideas on Cost Competitiveness and Sustainability. I hope the readers would love to go through it.

CMA (Dr.) A S Durga Prasad
President
The Institute of Cost Accountants of India

Chairman's Communiqué

It gives me an immense pleasure to present before you this new ***e- Magazine*** of the Institute on ***"Cost Competitiveness"***. It comprises of some case studies, interview of some eminent persons and a few innovative ideas related to Cost Competitiveness.

Having the lowest costs is not a guarantee of market success. We see Cost Competitiveness as a level of operation that allows an organization to go on winning sales at a price that generates a sufficient level of return both for stakeholders and for the investment needs of the business. Cost Competitiveness should not overlook quality of the product or service offered just for the sake of competition. Rather, it should aim at elimination of wasteful elements in the process and maintenance of performance.

The Institute of Cost Accountants of India is the only recognized statutory professional organization and licensing body in India specializing exclusively in Cost and Management Accountancy. 'Cost' is our forte. So we are presenting this issue with the aim to share innovative ideas and strengthen our knowledge base which would be highly beneficial for our members and society at large. Its versatility and accessibility would overpass the gap between Industry and Government. This magazine would be beneficial for accelerating socio-economic growth through Cost Competitiveness.

I would like to express my heartfelt thanks to my fellow members of the Research, Innovation and Journal Committee, the eminent contributors and the entire research team of the Institute for their sincere effort and support to publish this bulletin in time.

I am sure the readers will find the e-Magazine effective and would love to go through it and I also request them to put forward their valuable suggestion towards improvement of this e-Magazine in due course.

CMA Manas Kumar Thakur
Chairman, Research, Innovation & Journal Committee
The Institute of Cost Accountants of India

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Shri D S Rawat

Secretary General,
The Associated Chambers of Commerce and Industry of India

Q. *How cost competitiveness helps to increase the overall competitiveness of the country and how it affects the organizational growth & overall economic growth?*

A. Cost competitiveness helps an organization to achieve the status of cost effectiveness which results into producing value for money products. At a large scale when companies become cost competitive they contribute in making the country cost competitive in the international market. When companies reduce the cost of a product or a process they can have extra funds in their hands to spend on other important activities such as IT infrastructure, machinery, best human resources, quality management which leads to the organizational growth and ultimately to the overall economic growth of the country.

Q. *What should be the role of Government when an entrepreneur designs its cost competitiveness strategy?*

A. An entrepreneur, who is adopting cost competitiveness, is also contributing towards the country's cost competitiveness. In other words he is helping the country to emerge as the global economic leader. Government should also play a vital role in the designing of an entrepreneur's cost competitiveness strategy. Government should extend subsidy to those entrepreneurs in the purchase of Plant & Machinery, Government should also ease the process of quality control certification and make the tax structure lenient. Government should promote these products in international market so that demand of the product could be increased.

Q. *Based on your observations, do you think that current strengths of the members of the company are sufficient to cope with competition or need a change?*

A. The core competency of the organization plays an essential role to achieve its objectives and its strengths complement its core competency in a way that organization could cope up with competition. However, According to the changing dynamics of the market, there is always a scope for the change for the improvement. Strengths can be further improved to make the organization more competitive in the market.

Q. *In terms of long term growth and sustainability factors, how does cost competitiveness matter with respect to the organization?*

A. Cost competitiveness is an essential factor in terms of long term growth and sustainability of the organization. It saves money for the organization which could be utilized in other important activities such as technology up gradation, long-term investments, infrastructure etc which can take the organization to new heights.

Q. *How can stringent cost control on infrastructure and other facilities affect production cost efficiency?*

A. Every penny invested in the infrastructure has an impact on the cost of the production. The cost control on infrastructure will reduce the fixed cost of the organization and ultimately will increase the production cost efficiency.

Q. *In order to obtain a fair view about the performance of the organization, how to position the cost aspect from the competitive point of view?*

A. Today's cut throat competition has left no room for cost ignorance in order to obtain a fair view about the performance of the organization. The cost aspect should be kept on top priority from the competitive point of view. At the same time quality should also not be kept at low priority. Both aspects play a vital role in the today's competitive world.

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Impact of Cost Competitiveness to bring Sustainable Growth of Business

Shri Rajeev Mehrotra
Chairman & Managing Director
RITES LTD.

Q. *In your opinion, what are the major driving factors of a country's competitiveness? What is the position of India in this regard?*

A. The major driving factors for any country to retain its competitiveness vis-à-vis others are availability of reliable infrastructure to create capacity for production and services, availability of competent manpower along with adequate system support and data monitoring, quality of output including quality of intermediary processes etc. Further, country needs to leverage its embedded strength in terms of natural & human resources.

However, for a country to remain competitive in long run and increase its overall productivity, focus is also required to ensure sustainable & inclusive growth, have robust regulatory framework in place and provide mechanism for innovative financing.

In Indian perspective although lot of developments have taken place in last two decades in creating infrastructure and availability of trained manpower, still it is not at par with facilities available to companies in other developing economies like China, South Korea etc. Our focus has been on service based industries rather than production based industries.

The manpower base in India is exposed to latest IT and other communication & management technologies, including financial system and banking system. A strong cost management system plays a vital role in maintaining cost competitive edge on sustainable basis. Focus on manufacturing sector and in creating enabling infrastructure will definitely create competitive edge for Indian companies.

Q. *How is cost competitiveness beneficial to the profitability of the firm?*

A. The cost competitiveness includes a comprehensive range of production facilities to monitoring and controlling costs, timely decisions regarding appropriate technology and implementing projects of appropriate size and technology. Also, to be cost competitive, a firm has to eliminate the inefficiencies in its business processes on a continuous basis. Put together the industry achieves and maintains cost competitiveness. In the global scenario, the profitability pre-supposes a competitive edge and will definitely create value for various stakeholders.

Q. *How does cost competitiveness help the industry to crystallize thinking and build systems within the company to minutely capture and evaluate the value of all the resources?*

A. With maturity and experience gained within a industry, best practices and systems emerge and would drive individual firm to attain the quality benchmarks. Industries with experience identify strategic resources & plan for their effective deployment.

The impact of various resources used in ultimate delivery of goods and services is a complex chain of events and processes. An efficient system requires that the data at each stage is reliably captured, timely and professionally analyzed and corrective actions taken accordingly. Such an approach though may appear in the beginning bit exhaustive, but it can create robust internal monitoring and decision support system. The impact of change in inputs, variations in prices and quantities, changes in design can be captured online. Such systems also help in evaluating contribution from different components and evaluate their impact.

Q. *How do you evaluate your organization in this context?*

A. RITES is a global consulting company handling projects in various infrastructure sectors and spread over locations in several countries. Primarily, being a consultancy organization and think tank for key national infrastructure initiatives, it enhances its value addition in project delivery by leveraging strong knowledge base developed overtime. The systems have been so designed that not only at the time of bidding reasonably correct estimates can be prepared, but also during implementation, all the physical and financial bidding parameters, direct and indirect costs, profitability and risks are known all the time. The business unit heads are able to take corrective actions in time and manage resource allocations. The top management can effectively manage the company / ongoing projects by only focusing on exceptional items.

Q. *For deriving the real value of an organization, what will be the focal point of managing costs at an organizational and transactional level?*

A. The principles of cost management provide adequate solutions to develop focal points for identifying and managing costs at different levels in different business situations. The business environment and internal set up of the company, nature of business etc. will broadly derive the cost management at organizational and transactional levels. The business offers are designed so dynamically to ensure that the pricing is driven by line of business, long term clientele business perspective, diversification plan and maturity of business segment. For example, as a consulting company, at the organizational level, the contribution from all the divisions are monitored to ensure that the targeted levels are retained or bettered but at the divisional or transactional level, the control rests with divisions to see the compliance by individual projects or groups and also the overall impact collectively.

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Cost Management and Competitiveness in an Organization

Shri Asim Kumar Mukhopadhyay

Vice- President (Finance)

Tata Motors Ltd

Q. *For deriving the real value of an organization, what will be the focal point of managing costs at an organizational and transactional level?*

A. Real 'value' includes value created not just for the company itself but also for all affected stakeholders like suppliers, employees, customers and society at large. That is how sustainability is achieved and that is why many organizations have started including 'sustainability' in their agenda and value its significance. The organizations which do not heed to this business philosophy, over a long term, start losing relevance.

Also the current environment is such that the business dynamic are changing overnight, markets are getting more fragmented, greener initiatives are presenting new challenges, customers are demanding better than ever services and products and above all compliance to the many new regulations and laws is getting tougher. The bottom line is that not much has remained in your control - except one thing –'cost'. Hence, managing cost at all levels has become of paramount importance for the survival of a company in the present times.

The main reason to establish any firm is to avoid some of the transaction costs of using the price mechanism. Thus the focal point of managing costs at an organisational level is discovering relevantcosts and reduce them (keeping in mind these can be reduced but not eliminated). At a transactional level, standardisation and expense management are two focal elements for value creation. Standardisation plays a major role in lowering transaction costs when various links in the production chain are to be connected. It decreases the likelihood of miscommunication and makes drafting of, and negotiating on contracts easier. It also enhances marketability and fastens turnaround times.

The second element of managing costs is proper expense management. It refers to a system deployed by a business to process, pay and audit employee-initiated expenses. It includes policies and procedures which govern spending as well as the technologies and services utilised to process and analyse the data associated with it. Expense-management automation is the means by which an organisation can significantly reduce transaction costs and improve management control while logging, calculating and processing corporate expenses.

Like in many manufacturing industries, most of cost (as high as 80% in some cases) gets built up at the designing stage. Hence, due care and rigorous efforts need to put in lower one's cost base as much as one can. A clear cost target setting – whether, for the whole organization, product, or even at activity level- helps.

Firms also need to start viewing their offerings, whether products or services or their combination, in terms of how much value they provide to the end user. This way they could also arrive at a sustainable cost basis while creating value for all.

Saving cost is like running a tight ship; even a *single leakage can sink a mighty ship!*

Q. *How can India become globally competitive by implementing cost competitive strategy?*

A. Ever since industrial revolution, we saw the emergence of pockets around the world with global dominance in the trade that they would do. Cotton fields in Americas, coal mining in Pittsburgh, handlooms in Manchester, etc.

These were majorly resource based. But as resource capacity becomes globally available at low cost, its competitive value declines. The standard metrics of competitiveness that emphasize cross-border trade in goods no longer capture how and where value is created in the 21st century. Also due to technological advancement and human intelligence quotient today one can gain global competitiveness even if one does not possess proximity to the raw materials. Jack Welch, ex-CEO, General Electric once said, *"The real treasure of India is its intellectual capital. The real opportunity of India is its incredible skilled work force."*

India has already improved by leaps and bound in various sectors like Information Technology, Diamond processing industry, Textile, etc., where it now commands a global presence and respect. Looking back at why India succeeded in these businesses, one cannot ignore part that was played by cost leadership that India had to offer all along. Labour cost arbitrage was just one part of it. But this was on offer by many other countries as well. Once India began to make its presence felt and then subsequently went on to build a strong brand through value addition, adeptness in providing out of box solution, proficiency to customization to fortress its stronghold over cost effectiveness.

Thus, it would not be prudent to just look at being cost competitive to achieve dominance in market all over the globe. Cost is just one of the factors - an important one.The winning nations today are the ones that apply a 3-pronged strategy – cost leadership, differentiation and focus. This requires nations and thereby its firms to consistently and constantly innovate and invest wisely. Historically, it has been seen that cost leadership is not permanent and is lost in the long run because of innovation, or process reengineering by the competition. Also competition tries to focus on product differentiation to take the market away from your comfort zone where you have a cost leadership; thus, decimating your competitive advantage. Consider assessment of nine Asia Pacific countries as potential offshore service locations - India is the clear global leader by revenue, while China is the most serious challenger by scale. Bangladesh, Indonesia and Vietnam are continuing to gain regional traction for offshore service delivery as they are cheaper destinations. To beat the competition India cannot rely only on cost competiveness, it requires differentiation (build on quality resources etc.) and focus (refocus on the core capabilities of higher-end IT infrastructure, business process services etc.) As far as India and its future in global competitiveness is concerned it can be said that

"We have to continually be jumping off cliffs and developing our wings on the way down."

Q. *How does cost competitiveness cater to create the economic wealth of an organization?*

A. Economic value addition is both a measure of value and also a measure of performance. The value of a business depends on investor's expectations about the future profits of the enterprise. A sustained increase in economic value addition will bring an increase in the market value of the company.

As a performance measure, economic value added forces the organization to make the creation of shareholder value the number one priority. Stiff charges are incurred for the use of capital. Organizations focusing on economic wealth addition are changing the way managers run their businesses. When business decisions are aligned with the interest of the stakeholders, it is only a matter of time before these efforts are start reflecting into better performance and continued sustainability.

Michael Porter has said that wealth is actually created in the microeconomic level of the economy, not by macroeconomic policies – the latter only *"aid"* in wealth creation. Wealth therefore can only be created by firms. The capacity for wealth creation is rooted in the sophistication of the operating practices and strategies of companies. Attaining cost competitiveness as one of the strategies increases the capacity to create wealth. The core idea is to induce cost competiveness as a strategy and not as a tactical plan. This is especially true for companies that are in cyclical businesses. Also economic meltdowns are becoming harsher than ever. Sometimes surviving the downturn may be the most important thing for a company to do. Cost competitiveness can go a long run in protecting the company's future. More agile and nimble the company, more are the chances that it would take in the pain and be ready for the market to revive.

Q. *Do you think that current strengths of Indian Auto companies are sufficient to cope with the presence of global companies or need a change?*

A. In the recent past, India has seen many major auto players foraying in the domestic market.
India's automotive industry is the key driver of our growing economy. It plays a pivotal role in country's rapid economic and industrial development. The automotive industry comprises of the automobile and the auto component sectors. It includes passenger cars; light, medium and heavy commercial vehicles; multi-utility vehicles such as jeeps, scooters, motor-cycles, three wheelers, tractors, etc.

In India, automotive is one of the largest industries showing impressive growth over the years and has been significantly making increasing contribution to overall industrial development in the country. Presently, India is the world's largest manufacturer of two wheelers, fifth largest manufacturer of commercial vehicles as well as largest manufacturer of tractors. It is the fourth largest passenger car market in Asia as well as a home to the largest motor cycle manufacturer. The sector has shown great advances in terms of development, spread, absorption of newer technologies and flexibility in the wake of changing business scenario.

The Indian automotive industry has made rapid strides since de-licensing and opening up of the sector in 1991. It has witnessed the entry of several new manufacturers with the state-of-art technology, thus replacing the monopoly of few manufacturers. At present, there are more than 16 manufacturers of passenger cars and multi-utility vehicles and more than 9 manufacturers of commercial vehicles. The norms for foreign investment and import of technology have also been liberalized over the years for manufacture of vehicles. At present, 100% foreign direct investment (FDI) is permissible under the automatic route in this sector, including passenger car segment.

One significant conclusion that we can come to is that global competition is here to stay. Therefore, all Indian auto companies need to stay competitive to remain relevant in the current times. They may not have access to higher technologies and intellectual properties that their foreign peers may possess but they would do well to keep utilizing their knowledge of the current market and their customers.

In our opinion, current strengths of Indian Auto companies are sufficient to cope with the presence of global companies. With the granular knowledge of the Indian market, years of presence and strong connect with the users, Indian companies have built a relationship with the consumers. But this should not result in a lackadaisical approach towards continuing to strive hard and innovate. Cost competitiveness would remain at the heart of this. Understanding consumer and providing not just good products but also great services along with it should ensure that the Indian auto companies keep maintaining the lead that they have over their foreign counterparts.

A well laid down, progressive national level manufacturing policy which lets the state play a more enabling role in the development and growth of the Indian auto & auto ancillary industries would be a big help.

Q. *What in your opinion are the key drivers to be cost competitive in Auto industry?*

A. Like in many manufacturing industries, most of cost (as high as 80% in some cases) gets built up at the designing stage. Hence, due care and rigorous efforts need to put in lower one's cost base as much as one can. Targets need to be in place to arrive at the products with right positioning for the right customer providing right set of features. Any divergence from these would lead to lower returns on the costs incurred. Automobile sector is a capital intensive industry with a long lead time on returns made in the sphere of research and development. Hence, a clear strategy can go a long way in defining the future of a company. Modular approach to capacity building and flexibility of production of different configurations on the same line can be a boon for companies during lean periods when capacity utilization may drop. Also, it would save on the cost front.

Research in new materials and adaption of technological developments from around the world can help a lot. For example, the high-tech features that we provide to our customers in defense segment can tomorrow be used for general public.

Q. *Does public-private partnership enhance cost competitiveness?*

A. Public-private partnerships (PPPs) hold great promise for improving public services for the poor in emerging markets. But charting the political waters, balancing the needs of governments, consumers, investors, and lenders, and making the transaction transparent and sustainable are challenging tasks and not for the faint of heart.

The essence of a public-private partnership arrangement is the sharing of risks. Central to any successful public-private partnership initiative is the identification of risk associated with each component of the project and the allocation of that risk factor to either the public sector or the private sector or perhaps a sharing by both. Thus, the desired balance to ensure best value (for money) is based on an allocation of risk factors to the participants who are best able to manage those risks and thus minimize costs while improving performance. Cost competitiveness is raised as PPPs provide an organisation the capacity to raise capital at a low cost. As these programs cover alternative procurement and payment models (eg. toll and availability payments), they can reduce costs, improve project quality and provide additional financing options. But practical experiences tell us that many PPPs suffer from cost escalations, delay in completion, missing deliverables, etc.

A central strong leadership that is transparent and fully able to guide through a complex project is what is needed. Due to the presence of many stakeholders with different set of interests, a closer monitoring is required for PPPs.

Public-private partnership also provides an excellent opportunity to learn. Different types of firms come together and get a chance to work together. They learn each other's practices and processes and then go on to follow and develop the best practices. A lot of cost competitiveness also comes from the resulting size of the mega projects that PPP usually work on. All-in-all there is a large scope for learning and cost competitiveness from public-private partnership.

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Case Study

Towards a Sustainable Development: The UltraTech Synergy

By Dr. Sreehari Chava

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The Modern Cost Manager extends the perception of cost to every resource that is consumed in the process of value addition. To that extent, Cost Accounting is an enabler device that facilitates the management of resource utilisation and resource conservation while manufacturing a product or delivering a service. The entity gains competitive edge where the dual functions of resource utilisation and resource conservation are carried on to optimality.

UltraTech Cement (Grasim Industries Limited), an Aditya Birla Concern, is a Rs.27, 900 crore company with a reported net profit of Rs.2704 crores for the financial year 2012-13. The Company traces Environment Conservation as a catalyst for Sustainable Development. The company, over the last couple of years, carved out the environmental challenges into a synergy of growth with responsibility that leads to sustainable development. In the process the company throws up case based learnings to the modern cost managers in terms of alternative fuels, alternative raw materials, alternative power, alternative routes, water conservation, and so on.The company brought out its 'Sustainability Report 2010' highlighting the theme "Alternatives in Action". In its Approach to Sustainability, the report states "The Company utilises the Sustainability Report as a tool to display its efforts towards driving a triple bottomline agenda: the Planet, People and Profitability…… All this is done with a focus on alternative solutions, and discovering new avenues to promote its sustainability agenda." That is how Bottomline Profitability is correlated to the Environment and a plan is laid for a cost competitive future well ahead of the other peer players.

In its Annual Report for 2010-11, the Company highlights its thrust on use of alternative fuels to reduce consumption of fossil fuels by substituting these with wastes from other industries. The Company is reported to have saved using coal by recoursing to alternative fuels such as processed municipal solid waste, agro waste, tyre chips and used polythene and plastics. In 2009-10, the Company substituted the use of natural resources with 20,000 tons of waste materials as fuel, equivalent to 10,000 tons of coal burning every day. In the year 2010-11, the Company has used 70,305 MT of alternative fuel, of which 43,946 MT is bio-mass, which has saved nearly 42,000 MT of coal use. In the year 2011-12, the Company has used 70,744 MT of alternative fue, of which 28,717 MT is biomass, which has saved nearly 42,000 MT of coal use in the year.

On the material front, the Company opted for a conscious decision to reuse waste in their processes across the cement plants. The use of recycled material (waste reused) as part of total material consumption is stated to be the order of 14.61% of 2010-11 and 13.76% for 2011-12 leading to substantial conservation and savings by all means. The Company is reported to have used alternative raw materials from industrial waste of 83,86,382 MT for cement production in the year 2011-12 which has in turn resulted in avoiding usage of natural raw materials.

In relation to energy conservation, the Company has identified the use of the renewable energy sources as an area of focus. The Company has an installed capacity of 400 KW photo voltaic cell based on solar power plants in its various plants as of 2012. The Company is stated to be in the process of adding further capacity in its various plant locations.

The Company recognises the sea route as the most cost effective and environmentally friendly transport for delivering cement and clinker in the coastal and export markets. Company's Units at Kovaya and Jafrabad in Gujarat are among the largest users of shipping in the cement industry. These Units also receive incoming raw material and fuel sources such as gypsum, iron ore, coal and petcoke at its captive berth.

Water is a scarce commodity in the Indian context. The Company is focusing on reducing water consumption in all its cement units. The installation of bag house in the raw mill and air cooled condensers in the thermal power plant are major steps taken. The Company envisages water conservation of about 9 million M3 per annum through air cooled condenser in the thermal power plant. The pits created after mining of limestone have been converted as storage of rain water for use of Company's Units and the nearby community. These water bodies help to maintain the biodiversity of the area. Over 12% of its total water demand is met by recycling of waste water. At all integrated Units the treated water from the sewage treatment plants is used for horticulture gardening, cyclone cooling and dust suppression is common practice. At most of the Units, there is zero water discharge.

It is reported that the Company's approach to technology-selection, inherently evaluates water consumption over the lifetime of the equipment as one of the major criteria for adaptation of any technology.

In the words of Kumar Mangalam Birla, Chairman, the Group's Sustainability Vision is:- "By 2017, the Aditya Birla Group endeavours to become the leading Indian conglomerate for sustainable business practices across its global operations, balancing its economic growth with environmental and societal interests. This vision provides a common guiding principle as well as an operating framework for all our businesses".

On the profit dimension, i.e. economic value added, the Company is stated to have grown 20 times in revenue in the past 17 years; and during the last one decade, the CAGR in EBITDA has been 19%. And there lies the Cost Competitive Edge of the Ultratech!

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Case Study

Cost of Inefficiency and Revamping of Modern India Limited

By Prof (Dr.) D. Mukhopadhyay

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Backdrop of the Case:

Modern India Limited (MIL), a multinational firm engaged in manufacturing of alternator parts(P1, P2, P3 and P4) of generator for last fifty years. The product of the company has international market and it leads in term of cost efficiency and quality management. The company has manufacturing units in UK, USA, Japan, South Africa and Australia besides India. The company's financial performance during last five years is sluggish and depressive. All the manufacturing Units across the globe are functioning as individual Strategic Business Units(SBUs) and they compete with one another. However, they work on the principles of goal congruence. Each SBU is headed by a General Manager (Operations) and the organization structure of the company is of pyramidal and traditional headed by CEO Cum Managing Director. There is intra-SBU competition and one SBU can exercise option to buy input from another SBU or open market. Transfer Pricing Mechanism is in place. The company has four directorates and they are Marketing, Operations, Finance and Human Resource and all the board members and their immediate subordinates sit in the Headquarters of the company. The leaders of the SBUs function as an individual decision making entity and report to the CEO thorough the concerned directorates. The company works on the strong guiding principles of focus, cost leadership and product differentiation. The firm has a full -fledged Total Quality Management(TQM) cell and the total quality management cell of the company was very active and efficient at the initial years of operations and it did never make any compromise in quality control and quality management of the product keeping in view the international standards and parameters. This was the inherent strength of the company. The company was always watchful on market standing, productivity, management of financial resources, performance of the managers, attitude of the staff, professionalism, surplus creation and honouring corporate social responsibilities. These are the preambles of the company on which it is founded. But the company is not in a position to make its way in the roads of globalization. The case of the company's performance in totality can be understood from the foregoing account as is made hereunder.

Marketing Functions Perspectives:

The Marketing Directorate is headed by Director (Marketing) assisted by GM (Marketing) at the corporate level. The company is having a downward trend in sales over the years. The budgeted sales for each SBU is 12, 000 (in P1:P2:P3:P4: 1:1:1:1 Ratio) Order received for sales during last five years are as in Year-1, it was 14,000 units, year-2 it was 12, 000 units, year-3 it was 10,000 units, year-4 it was 9, 000 units and year -5 the order received for 7, 000 units. Actual orders received were almost in the above ratio in last five years for the products of the company. The marketing directorate placed its arguments in favour of downward order that both quality and cost in particular and selling price in general are having adverse impact on fulfilling sales target. Earlier, the company was the market leader for the products mentioned above. Now market is very competitive (and practically it became a 'red ocean' now) and after sales service are offered free for three years to five years by the competitors whereas MIL offers only one year after sales free service. The pricing policy is not reviewed for last two years. Market Research (MR) cell is not in a position to work in proper direction keeping pace with at least for the purpose it was created. The marketing information reports generated by the marketing wing of the company both at SBU levels as well as corporate levels reach late to the board for taking appropriate measures and decision. Director (Marketing) does not have sufficient information for reviewing the performance of the sales force periodically. Sales are the part and parcel of the marketing directorate. Advertising and Sales Promotion Budget, according to the CMA of the company, is devoid of justification in terms of result. The incentive for sales force is hardly linked with target achieved by the sales and marketing people. Sometimes, marketing people blames production people for untimely delivery to the customers. There is continuous complaint concerning production of sub-standard product which does not conform to the true requirements of the customers.

Operational Functions Perspectives:

The Operations Directorate of the company is headed by Director (Operations) and assisted by GM (Operations) at corporate level and all the SBUs are headed by GM (Operations) as already mentioned elsewhere. The engineering works of each SBU has 585 uniformly employees under different hierarchies starting from Operational Managers. It follows a scalar chain of 1:8 and it is maintained that 1-8-64-512 i.e. one GM(Operations), eight Dy. GMs, sixty four Managers and five hundred and twelve Operational Managers are approximately there in the payroll of a SBU. Operations Directorate is also controlling authority of Purchase functions and Research and Development and Research and Development Cell is responsible for value analysis and value engineering including product designing. Cost of product is alarmingly high and cost reduction and cost control policy and mechanism is in place in paper only. This is the age of automation and this hardly receives any priority in the Operations Directorate.

Employee cost is almost entirely fixed and nothing other than material cost is variable. Overhead is semi-variable and it may be within a range of 20% as variable and remaining 80 % is fixed. The Cost & Management Accountant (CMA) is of the view that activity based costing can bring about correct product costing and hence in product pricing. Each product should be burdened with its own cost and not that of others. It is the general tendency of GM (Operations), SBU-In-charge, to overrule the recommendations and suggestions of the CMA posted at the SBUs. The material cost variance, labour cost variance and overhead variance in most of the times are adverse and the principles of management by exception are the allergy of SBU-In-charge. Purchase manager is to work in conjunction with stores manager, production managers and finance managers and production managers are required to work in conjunction with marketing managers. Scientific inventory management techniques can help in managing inventory carrying cost and inventory ordering cost according to the CMA. Purchase manager can help in getting reasonable discount in following effective purchase policy. Work study was undertaken by the SBUs five years back and the recommendations of work study group are under the cover of dust.

Finance Functions Perspectives:

The Finance Directorate is headed by Director (Finance) and CFO and is assisted by GM (Finance) at corporate level and Finance Function at SBU level is headed by Dy. GM (Finance) who is essentially a qualified CMA as per the policy of the company. According to the periodical report generated by Finance Wing, cash flow is very weak and there is irregular flow of revenue to the coffer of the company. Collection cell is under the administrative control of Marketing Directorate and functionally responsible to the Finance Directorate. It violates the principles of unity of command and as result it causes an administrative problem for securing accountability and this has been brought to notice of the HR Directorate over time and again but no workable solution is generated so far. Financing working capital is dependent of the strength of cash flow. Purchase Department fails to secure more credit period from the sundry creditors than the collection period allowed to sundry debtors and the same is being practiced by the collection department without any review. The company is contemplating for diversification of its business from manufacturing alternator parts of generator to manufacturing of industrial cranes and for this purpose it needs injecting both debt and equity in terms of Rs.1,000 crores. But it is afraid as to whether people would subscribe to the equity since for last five years rate of dividend payment is marginal even less than that of savings bank interest rate. Currently the company has a capital base of Rs. 2,000 crores out of which 40% is invested in working capital and remaining 60% is locked up in physical and infrastructural assets.

The CFO of the firm is worried that operational cost is with upward trend and revenue earning is with downward trend and it is a very difficult situation to match revenue with escalating expenses. An Earnings per share is abruptly low and it is difficult to earn the confidence of the investors under such circumstances. There is accumulation of book debts and inventory and stores and this disturbs the short term liquidity of the business. The cost structure in terms of the cost of sales of the product comprises of 50%-material, 30% employee costs, 20% overhead and 5% of the cost of sales hardly contributes to profit. CFO feels that abnormal loss in material handling and overhead needs to be controlled and the performance based incentive scheme for the employees should be adopted in order to make the firm financially solvent.

Human Resource Functions Perspectives:

The HR Directorate is headed by Director (HR). The Company has a full-fledged Human Resource Directorate and it deals with recruitment, training and development and promotions of the people of the organizations in general. The HR Directorate functions and monitors the HR Budget as is framed by the company. There is centralization of HR Policy. It is the responsibility of the GM (HR) at corporate level to act as the chief coordinator among the SBU level HR Managers. The SBU HR Managers prepare HR Budgets annually and the same is incorporated in the Master Budget of the Company. It is has been observed that a substantial portion of the HR budget remained unutilized during the panned period and the GM (HR) could not justify the non-utilization of the HR Budget. Budget proposal is placed by SBU HR Managers and the same is forwarded by the GM (Operations) to Headquarters of the company located at Mumbai, India for adoption. Moreover GM (HR) takes lot of time to communicate the approved HR budget to the SBU HR Managers and SBU In-charges. The world is changing very fast keeping pace with advancement of science and technology. Staff cost is 30% of the cost of sales in general and every employee has to contribute positively to growth and prosperity of the company. The people of the organization have to work keeping in view of importance and significance of economy, efficiency and effectiveness. Non performers have to be identified and the company does not have a time-honoured mechanism and parameters for measuring the efficiency of the people. The company HR Policy is back dated. It is observed that a person who joined as Foreman/supervisor remained in the same position during last twenty or more years. The employees at all levels are found demoralized and de-motivated. The cost of inefficiency burdens the pricing of the product in particular and the firm in general. The people of the organization are concerned with mission, vision, objectives and goal of the company only in paper and it lacks initiative in translating vision into action and action into result. The leadership of the company is found to bureaucratic and sometimes it is autocratic. Chain of command and control is centralized at corporate level. There is mounting court cases between the unhappy workforce and the firm. The company is functioning in a closed ended system.

Conclusion:

It is evident from the above that the firm in our Case is ambitious for expansion of the business in one hand and on the other hand it is not in a position to manage the existing business in cost effective manner. It fails to generate reasonable rate of return on capital employed, could not pay good dividend, working capital financing is weak as a result of feeble cash flow, burdened with inefficient workforce and attributed with alarming rise in cost of production and attributed with declining trend of earning revenue. The cost of inefficiency is yet to be worked out. The Total Quality Management (TQM) hardly works. Internal failure cost, external failure cost, appraisal cost and correcting costs are major components of TQM but they remain unreported in most of the time. There is huge gap between contemplation and action. An organization means people and it fails to deal with its people in time-honoured conducive manner that can inspire and motivate the workforce of the company. The CMA has been giving continuously alarming bell but the management does not give due attention to it. It is now high time to draw the existing balanced scorecard and the budgeted one for the given firm. Both the principles of management by objectives and management by exception need to be made workable in cohesive manner. The sustainability and survival of the company under fierce competitive environment needs to be ensured. The CEO & Managing Director is not getting relevant information for the purpose of formulating appropriate strategy. Management Information System (MIS) is inactive, inefficient and ineffective. The whole organization is plagued by inefficiency and they ultimately have failed to deliver the result. Under the circumstances, the CEO & Managing Director requested the CMA as the business strategist to submit its report on the overall functioning of the firm incorporating its recommendations for revamping, sustainability under competitive environment, honouring the claims of various stakeholders and complying with the requirement of corporate social responsibility of multiproduct-multinational firm as the present one. It also should suggest an efficient transfer pricing mechanism that would promote goal congruency in the organization on overall count.

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Be Innovative Be Cost Competitive.......

A. Energy and Cost saving in Mining Sector

Backdrop:

BESTECH, Canada delivers new Ventilation-On-Demand system for underground mines, saves significant energy costs. Optimising ventilation is not just adding more air but balancing several considerations to ensure personnel and equipment can be safely managed underground. The VOD systems can be cheaper to install and operationally robust.

Objective

- The innovation aimed to improve energy efficiency.
- Reduction of Operating cost.
- Reduce carbon emissions at underground mines.

Methodology:

VOD system enables the capacity to get air to where it is required, when it is required. The installation of VVVF drives reduces capital costs as the fans can remain the same. The VVVF drives can reduce vibration (if fans and bearings are well balanced) during changes in fan speeds in a VOD system. VOD systems can reduce shock losses and turbulence in the ventilation streams by reducing the velocity when the ventilation is not required. If VOD is implemented into the mine as it is developed, smaller ventilation shafts, fan installations, supporting infrastructure and capital costs are lower than a comparable flood ventilation system.

Applicability:

In 2012, India was the third biggest hard coal producer after China and the USA. Around 55 per cent of energy production in India stems from coal. Thus, this innovative approach can highly be effective and cost competitive for collieries in India.

B. *Lean Technique in Hospital sector- A Journey Ahead*

Backdrop:

Barnes-Jewish Hospital in St. Louis, MO, United States of America, used lean technique to speed up stroke care. With the help of this technique, average time between patients arriving and receiving clot-busting treatment dropped by 21 minutes. It would result to fast and effective treatment and curtail brain injury probability rates after stroke.

Objective:

The objective of lean technique is to curtail the unnecessary wastage of time and motion. As a result quality of service would enhance and cost per service would decline.

Methodology:

Using lean technique the hospital can identify unproductive steps such as inefficient patient transportation, task performed at a time rather than simultaneously etc. because this technique would facilitate to relook at what actions performed everyday.

It enables the competent authority of the hospital to formulate protocols of keeping only crucial steps that would add up value to patients care.

Applicability:

1. Emergency Ward
2. OPD

Emergency Ward:

Oxygen cylinder, Blood, life saving drugs, medical equipments and laboratory test facilities to be present at the bed side of the patients to get laboratory results within minutes, these moderations would ensure rapid diagnosis and treatment available for patients as soon as they arrive at the emergency department. As a result quality of service and the productivity of personnel would improve and time per patient would reduce.

OPD:

Queue management is a must for OPDs. A trained nurse should be appointed for each doctor, who would check the blood pressure, height and weight of the patients and arrange case report for the doctor. This could reduce time per patient and doctor can treat more patient than before as a result cost per patient would reduce.

C. The Impact of Activity Based Costing on Insurance Company's Performance

Backdrop:

Sun Life Insurance is an international insurance company in Canada. Several issues have led Sun Life to undertake the implementation of an Activity Based Costing (ABC) analysis. Increased competition, the introduction of new computing technology, and increasing client demands have caused margins to decrease and costs to raise. The increased costs and decreased per unit revenue have pressured management to seek to reduce costs significantly to maintain profitable operating results.

Objective:

- Cost Reduction
- Performance Evaluation
- Sustainability of business

Methodology:

The ABC system implemented within Sun Life Group Claims has helped to assess the "value" or utility of all the activities performed within group claims and realize significant reductions in operational costs within the claims processing areas. Sun Life has been able to perform extensive benchmarking analysis to determine how efficient and effective they are, compared with where they can be and has shown management where to concentrate the process improvement initiatives.

Applicability:

If Activity Based Costing can be applied in the Insurance sector of India, it would prove to be a cost effective approach for the following reasons:

- Reduce operating costs.
- Time management.
- Better settlement of claims.
- Benchmarking.
- Facilitate in Decision-making purpose.
- Better business performance.
- Business sustainability.

D. Cost Reduction Consultancy Services

Backdrop:

Consultancy services on operations analysis are well –known to the European food industry. They help the companies in cost reduction procedures by providing innovative ideas, and cost saving alternatives with respect to manufacturing aspects.

Objective:

- Consultancy service units facilitates in cost reduction and increase profitability.
- It flexibly assists companies with advising, training and implementation.

Methodology:

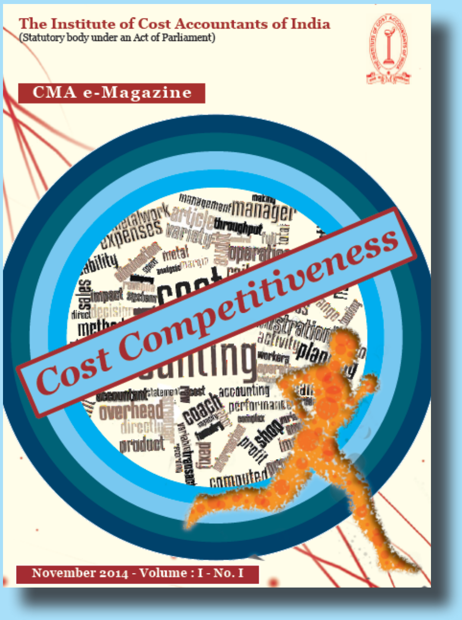
They assist the company manager who is under pressure to deliver top results in a short time by providing him with new recommendations, leads and ideas for technical cost reduction and increased profitability.

The methodologies that were carried out are as follows:

- Six Sigma Approach
- Lean Technique
- Innovative Cost Reduction Audit (ICR-Audit), a diagnostic tool, designed.

Applicability:

In a Business Group, if a separate unit for Cost Reduction Consultancy services can be set up consisting of an expert team, having in-depth knowledge of costing, then it would help to curtail cost and wastages, increase efficiency, productivity and profitability per department or Business units through continuous examination and applying suitable approach or techniques. It will also reduce the extra pressure of top managers in planning and bringing competiveness of their business.



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