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AN INDEPTH ANALYSIS OF THE COST MANAGEMENT TECHNIQUES FOR THE INDIAN FMCG COMPANIES

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Abstract:

Cost management is the process of planning and controlling the budget of a business. Being a form of management accounting cost accounting allows a business to predict impending expenditures which shall help reduce the chance of going above the preset budget. Implementing a cost management structure for projects can help a business keep their over-all budget under control. Several business intelligence programs, such as Hyperion, offer cost management software to help businesses monitor costs and increase profitability. While the software may help, it is not imperative that software is used when executing a cost management plan. We shall go through hypothesis testing with the help of primary data and secondary data collected via FMCG companies.

Keywords:

SCM, variance, EOQ, cost-benefit, strategy

Introduction

All the financials (Balance sheet, Ratio and Quarterly statements) portray a story in the form of secondary data which help us in drawing a conclusion for the above concerned sector. For an effective cost management strategy the company should focus on its overall cost reduction tools followed by delay of cash outflow (like outstanding expenses, suppliers) and stress on quick recovery of all cash inflow tools (like debtors, accrued income and prepaid). All other expenses should be as low as possible; the company can think of better substitutes if available. Emphasis should be mainly upon apt utilization of raw material and productivity of labour part because that forms the main ingredient of cost sheet. Logistical support and promotional tools forms of a secondary relevance in cost sheet.

Hypothesis of the study:

a) Strategic cost management identifies many purposes including accounting of cost to obtain product inventory costs or full costs.

b) Strategic cost management shall help FMCG companies to grow in tune with speed of change which is led by hyper-competition and longer product life cycles.

c) Strategic cost management is the responsibility of functional managers and not of the top management.

Analysis of the Primary data :-

The rationale for the increased significance of cost management concept differs among the firms studied. During the interviewing process, it became clear that all the organizations studied had cultures of cost consciousness, originating from the top of the organization (Board of Directors) through all levels and functions of the organization, and touching their suppliers/vendors as well. Rise in the price of the raw materials was found to be the prime reason for rise in cost management. Other factors were also voted but since raw material forms the basis and forms more than 70% of the total costs so a little rise in its prices would adversely increase the price at the end of the process. We have already summarized earlier that how responsibility for conducting cost management is spread within the core organizations studied. Each of the five organizations discussed has taken unique approaches to ensure that it has the cost analysis and cost modelling skills in place within its organization to support strategic decision. A number of barriers that organizations had to overcome, to be successful in strategic cost management. The list of internal barriers outweighs the list of external barriers. Internal barriers are in the form of Lack of accountability, Lack of immediate benefits and Lack of information systems to support analysis and tracking; whereas, External barriers are in the form of Economic downturn, Inconsistency in treatment of suppliers; swing from alliances to adversaries, Customers unwilling to share information and Suppliers unwilling to share information. It is hard to gain leverage when the demand is constantly changing that too in such a hyper-competition. So the prime reason voted was lack of immediate benefits which is quite impossible to gain in such an industry. So it has proved to be the biggest hurdle. The key external barrier to strategic cost

management is economic downturn. It may be related with India or with any foreign downside which shall obviously affect the Indian Industries. Economic downturn or depression we can call it adversely affects the cost and profits of any company. It is not about only FMCG but majority of the companies. Also every company here gets affected through downturn which is a business cycle. Strategic cost management success depends upon various factors which we have listed earlier like Hired trained professionals where needed, Implemented new processes, Cross-functional teaming and Supplier development. As per our primary data the cross functional teaming function has proved to be the key enhancer for strategic cost management. 100% of the companies said that they review their strategic cost management strategies on a monthly basis. Reviewing its quarterly or annually may hamper the company because of the stiff competition present in the current market. Reviewing the strategy at such a span edits the criteria and makes it more strong and valid. In such a process SWOT analysis also plays a vital role. Three out of five companies said strategic cost management basically revolves around cost-benefit analysis. Strategic cost management is all about how the cost of the company is changing and handling its variance if any. No doubt strategic cost management is also affected by value chain analysis and variance analysis but strategic positioning hardly revolves around strategic cost management as per my primary data. The probability of variance in strategic cost management is somewhere between 0%-25% as per our primary data. Four out of five companies revealed as per our primary data. Variance is the difference between the set benchmark and the execution. If the Executed strategy may vary from the actual set strategy some may be due to unavoidable situations and some which are purposely done due to lack of apt responsibility. That variance is measured by standard deviation. 90% of the FMCG companies said the variance is somewhere around 0%-25%. In this question we shall deal with its cause; the cause of the variance. Two out of five have said competitors strategy is the reason while the other two have said that the basic reason is the market in which they operate. Four out of five have reported that low price factor is the basic reason that consumers buy FMCG products. Consumers basic human nature is to get attracted towards low price available in the market. One has said that sales promotion is the factor. Sales promotion may be in the form of advertisements or free gifts or luring customers

externally in some way or other. As based upon hypothesis a suitable strategic cost management recommendation for a strategic FMCG company could totally de-emphasize the adoption of the new wave competitive cost management techniques. Four out of five companies have voted for it in the form of yes.60% of the sample data revealed that strategic cost management is a long run investment. The companies who believe this is running on a right track because every activity should be focused upon long term.To shift to a new strategic system is a constraint to many. Company is not ready to change its track of strategies because that shall lead to wastage of time and money. Two out of five have said that it depends upon the situation. Lower the change in cost YOY better it is. But actually it depends upon factors the cost changed. Variance means change from 2015 figure in the year 2016. Marico has highest 27.8 % cost YOY variance while HUL has a minor 2.6 % change. Reason may be high cost of raw materials or increased market expenses due to inflation or increase in sales may be another factor. Three out of five have said that they shall invest upon promotional activities to attract consumers in form of advertisement or free gifts. Consumer's basic nature is simple that it gets attracted towards external factors like promotion. People become aware of the product and the repeated advertisements lure them. More over schemes like buy one get one free and get 50% extra is another luring factor. The strategy of FMCG basically is dependent upon the cost factor. More the cost. Less competitive shall be the price and less number of consumers shall approach it. Everything works in the opposite direction. Less the cost more the consumers. The vital point is consumers are the king and the companies have to move and strategise in accordance to the customers mindset. The managers need to think like consumers and deeply understand about their perception of their respective brands.

Analysis of the Secondary data:-

A) Conclusion from the analysis of balance sheet comparison: -

Financial statements play a vital role in providing assistance to the secondary data for a research study. In accounting one should delay the payment as far as possible so that a larger Current liability is better and ultimately the cash outflow starts reducing. Quarterly payment can be made to suppliers and labourers and other expenses can also be delayed to increase the current liability

as far as HUL is concerned. No doubt inventory/stock is followed by the cash outflow but the company strategically can delay the outflow towards their suppliers, thereby increasing the stock without reducing the cash (working capital) immediately. Moreover for a quick outflow of inventory the company can adopt various sales promotional schemes like discount or gift vouchers or free gifts or next purchases coupons. Taking "ageing" factor into account Company can design strategies such as older the stock, lesser the price so that at least the cost can be recovered through it. Company can follow JIT (just in time) approach for more stock and lesser warehouse space. Obsolete stock should be disposed off. Company must ensure that WIP is processed and not stocked. EOQ (Economic Order Quantity) should be Followed. The Company should adopt an Ageing policy so that the goods shall not be stocked up and hence the current assets shall reduce. Moreover, LIFO or FIFO methodology can be adopted for a successful stocking policy and maintenance of store. Another strategy could be apt debtor management policy such that credit time period allotted to debtors is less which can reduce current assets to an extent. For good debtor management the company can follow debtor discount policy so that they are motivated to pay as soon as possible. Cash should be maintained at an optimal level. EOQ (economic order quantity) policy should be maintained so that over stocking can be avoided. Ordering levels should be frequently updated and average stock level should be maintained. Over stocking or under stocking both must be avoided.

B) Conclusion from the analysis of ratio sheet comparison:-

Ratios are not absolute but they are relevant enough to portray a good figure of the concerned company. High or increasing operating margin is preferred because if the operating margin is increasing, the company is earning more per dollar of sales. Cost reduction tools need to be adopted along with increase in sales revenue. Higher the turnover lower shall be the cost. It shall help strategize strategic cost management. Unnecessary product feature should be reduced. Second, negotiation could be brought into force. Third, offer quick payment for lower cost. Larger the imported raw material less shall be the command on its cost and supply thereby making the company more dependant and less flexible to change strategic cost management. Goods should be compared and thereafter the company should purchase from where the goods

are available at a cheaper rate. Logistics expenses also forms an important part of expenses column so the warehouse should be at nearest location from where raw materials are procured and at same time the outlet should be aptly connected to the market place.

C) Conclusion from the analysis of Quarterly statement comparison:-

Higher the income from operations more smooth is the strategic cost management frame. Dabur is at the best place and the poorest of all is HUL. Raw material consumption is more or less constant over past five quarters as per the quarterly statements. We can see a slight uptrend in it because of expensive labour available now-a-days, so the company has to pay more for the same labour work. Dabur which consumes highest raw material is taking highest labour work and similar applies to HUL. Administration and selling expenses -It should be as low as possible because it is an expense which is invisible. It is a semi variable cost.

Findings:

Combining both the primary data and the secondary data a finding has been made which is the vital and foremost point of this research study. The strategy of FMCG basically is dependent upon the cost factor. More the cost less competitive shall be the price e product of and less the number of consumers shall approach it. Everything works in the opposite direction. Less the cost more the consumers. For an effective cost management strategy the company should focus on its overall cost reduction techniques followed by delay of cash outflow (like outstanding expenses, suppliers)and stress on quick recovery of all cash inflow tools (like debtors, accrued income and prepaid). All other expenses should be as low as possible; the company can think of better substitutes if available. Since it is a long run investment to shift to a new strategic system is a constraint to many. The basic reason of increasing costs was raw materials. Rules need to be reviewed for labour unions such that they do not demand higher wages. Warehouse distance should be near to production area such that logistics cost is reduced. Company must have a back up a policy to handle high variance. Since in FMCG market consumers get attracted towards lower prices so the foremost thing that needs to be strategized is the cost factor which can be

reduced by inching down all the relevant cost overheads such that total cost reduces and operational profit increases.

Recommendations:

In marketing world it is said that the consumer is the king. The CEO has to bow his head in front of its consumers demand and their approach. More the cost, less competitive shall be the price and lesser the number of consumers shall approach towards it. Everything works in the opposite direction until there is some exception. Less the cost more the consumers. For an effective cost management strategy the company should focus on its overall cost reduction techniques followed by delay of cash outflow (like outstanding expenses, suppliers/vendors)and stress upon the quick recovery of all the cash inflow tools (like debtors, accrued income and prepaid/advances). The strategy should be focused on cost consciousness and not upon cost cutting. The suppliers need to be negotiated for a reasonable cost but no cutting of materials should be made. Reduce Import and increase usage of domestic substitutes. Goods should be compared and thereafter purchase from where the goods are available at a cheaper rate. Moreover inward transportation costs may be reduced to avoid adding up to the raw material total cost. It can be done by reducing the distance between suppliers and warehouse and the production house. All other expenses should be as low as possible; the company can think of the better substitutes if available. Second, negotiation could be brought into force. Offer quick payment for lower cost. You can achieve greater profits through more efficient use of the expense dollar. By increasing the average sale per customer, by effectively using display space and thereby increasing sales volume per square foot, by getting a larger return for your advertising and sales promotion rupee, and by improving your internal methods and procedures. Since it is a long run investment therefore to shift to a new strategic system is a constraint to many companies especially in FMCG. The basic reason of increasing costs was raw materials. Rules need to be reviewed for labour unions such that they do not demand higher wages unnecessarily. Just like a human life line even business have its lifeline and a cycle. Booms and depressions form a cycle. The company strategy should be to take extraneous advantage during boom period and to compensate the losses incurred during

depression. Raw material warehouse distance should be near to the production house and the finished goods warehouse should also be near to the distribution house such that the overall logistics cost is reduced. Company must have a backup a policy to handle high variance. Since in FMCG market consumers get attracted towards lower prices so the foremost thing that needs to be strategized is the cost factor which can be reduced by inching down all the relevant cost overheads such that total cost reduces and operational profit increases. Patience and long-term thinking is the way out. Cost should not be thought of as an expense rather it should be considered as an investment with future benefits.

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