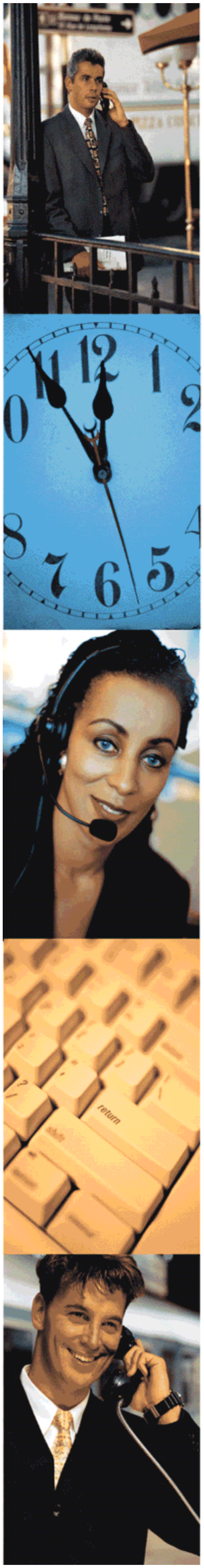

Avoiding the Death Spiral While Reducing Operating Expenses

A guide to make informed decisions about cost reductions while minimizing impacts on your customers

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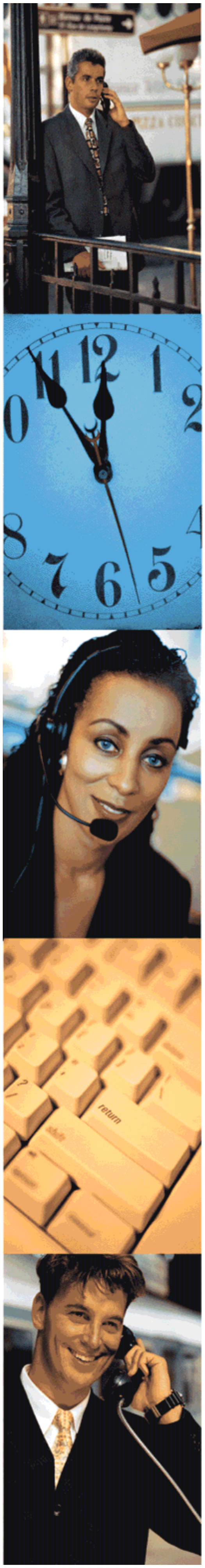


Avoiding the Death Spiral While Reducing Operating Expenses

One of the most complex challenges that business leaders face today is that of maintaining customer confidence while reducing operating costs. It's a business reality that when a company fails to make its revenue numbers, it has to take action to achieve (or regain) profitability. This white paper will share practical approaches that can be taken to reduce operating costs while minimizing the impact on the customer. In fact, why not go a step further by taking steps to increase customer satisfaction at the same time!

After all, the customer is the single source of the "current" revenue stream and represents a link to future revenue. If costs are cut in a way that negatively impacts the customer then you may very well enter a "death spiral." That is, you cut costs, the customer is negatively impacted and you have defections. Your next quarter's revenue numbers are off again. This results from the current economic environment (e.g. you are unable to sign new customers) PLUS the fact that you have fewer customers than last quarter. You again cut costs, the customer is negatively impacted and you have more defections. It's a vicious cycle. But, there is a better way…

Following are approaches that can be taken to reduce operating costs while maintaining customer confidence and increasing customer satisfaction:

- Cease activities that provide no value-add
- Implement efficient and repeatable processes
- Focus on product quality instead of new features
- Enable customers to self-serve
- Perform elements of the work with lower cost labor
- Segment the customer base and support levels
- Make informed decisions, not random cuts
- Cease big, expensive projects with long-term ROI
- Renegotiate vendor contracts

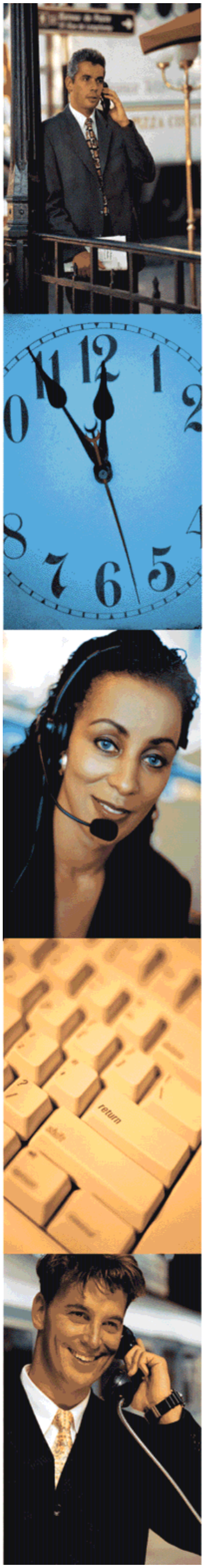
Each of these topics will be covered in detail, in the following sections.

If you make cost cutting decisions without considering the impact to your customers, you have lost sight of your current source of revenue. You may also be cutting off your future revenue streams. There are plenty of other companies that are more than happy to focus on your customer, namely your competition.

Could your competition be making decisions RIGHT NOW to forego the achievement of this quarter's profitability results (short-term thinking) and investing in ways to capture market-share to position itself for future profitability (long-term thinking) with YOUR customers? Something to think about…

Ceasing Activities That Provide No Value-Add

In the course of growing a business, each person on your team undertakes various activities which, at the time, make perfect sense to effectively deliver service to your customers. This could include policies, procedures, one-off databases, agreements with third-parties, etc. Over time, however, these can become outdated or no longer effective in the current business environment. When looking for ways to reduce operating costs while minimizing the impact to the customer, you are encouraged to "look here first." While you won't necessarily find a silver-bullet, each step you take to improve operational efficiencies contributes to the cause.



Let me provide you 2 examples from personal experience. A business that I was involved with had to take some serious actions to reduce costs and become more efficient, while at the same time making sure that our customers' confidence and satisfaction remained high.

Example 1 - Outdated Policy:
I had, quite serendipitously, come across a fax document that was developed as part of a customer authentication policy. I asked the dumb question: “What is this for?” To my amazement, I learned that “years ago” a policy was instituted where each new customer was required to complete a paper-based form with contact and related information, and fax it to our customer service team. I then asked: “What do we do with this document?” The answer (not so much to my amazement) was: “Oh, we file that away.” You know my next question: “Do we ever need to go back to that file to retrieve the document?” The answer: “No”. No further questions, I suspended that activity IMMEDIATELY. This saved us quite a bit of time. We no longer had to fax the document to each new customer, follow-up with the customer (time and cost of the long-distance phone call), receive the fax and file it. Not to mention, we made it easier for the customer to do business with us.

Example 2 - Subsidizing the Work of a Third-Party:
We had negotiated a contract with a third-party provider to perform elements of our overall service offering. Over time, this particular third-party was increasingly NOT pulling their weight, and the work was instead being performed (subsidized) by my customer service team. This initially went unnoticed, as the customer service staff just “sucked it up.” However, when the pressure was on to reduce costs this item bubbled-up, in a haphazard way, as a ripe opportunity to reduce work-load. What this required was our reviewing the original contract that we had established with the provider, quantifying the work that was being performed by our organization, when it should have remained with the third-party provider, and then working with the management team of the third party to hold them accountable to the original contract. Finally, we had to lock-in accountability on our own team for who would manage this third-party on a go-forward basis, because we had obviously not been paying attention to their performance and instead simply “doing the right thing” by servicing every customer that called in to our service organization.

The lesson from both of the above examples is that you are encouraged to consistently ask your team-members (on the front-line) the following questions:

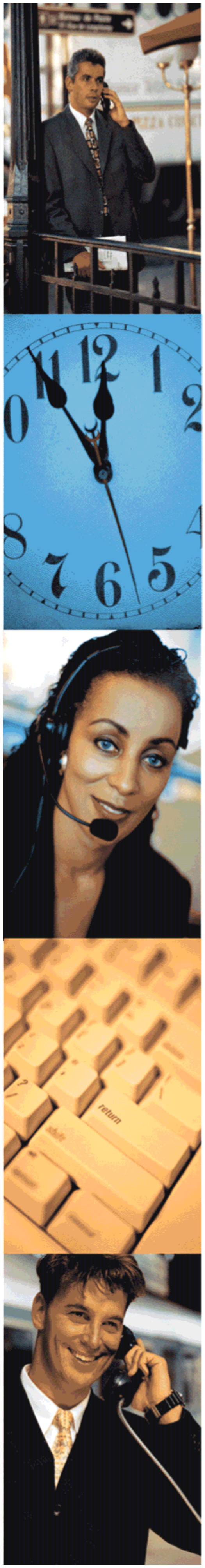
- What is in your way of delivering excellent customer service?
- If you were running this operation, what policies or procedures would you eliminate to save time and money?

Finally, the approach of “management by walking around” can be highly effective in this regard as you make your own observations about the working environment and the various interactions your team has with the customer. Guaranteed, if you haven’t done this in the last 3 to 6 months you will find “low-hanging-fruit” that is ripe for the picking.

Implementing Efficient and Repeatable Processes

Aligning your personnel to common business processes can have a dramatic short- and long-term impact on improving operational efficiencies and increasing customer satisfaction. Additionally, this will prepare your firm for scaling the business during the next wave of growth, which is sure to come. Some of the most common operational areas that you should consider defining and implementing repeatable processes include:

- **Order Management** - The activity of processing customer orders to ensure quality order fulfillment. This is where the proverbial statement "garbage in, garbage out" most applies.
- **Order Fulfillment** - The activity of delivering/installing your product/service per the customer order, ensuring customer acceptance which locks in your ability to invoice the customer.



- **Inquiry Management** - The activity of managing customer inquiries (email, web, phone) in such a way that the customer receives a consistent level of response regardless of the medium used to obtain service.
- **Customer Problem Management** - Aligning the entire organization to a common and proactive model for responding to customer problem reports, performing customer notifications when significant disrupting events occur, and ensuring management attention to avoid surprises.
- **Change (or Maintenance) Management** - Aligning your organization to a common model for performing maintenance activities on the service delivery infrastructure in such a way as to minimize or eliminate the impact this work has on the customer-base.

To be effective, your operational business processes must include, at a minimum, the following elements:

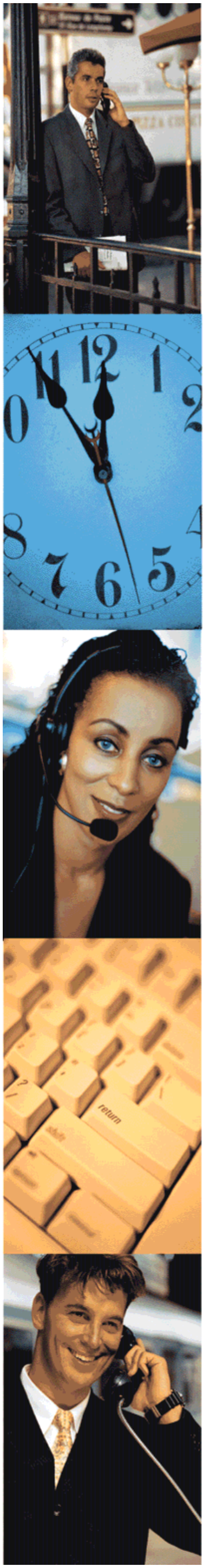
- **Executive Sponsor** - A senior executive that is committed to the success of the process, and performs periodic (monthly or quarterly) reviews to ensure process performance remains on track.
- **Process Owner** - A seasoned leader with the proven ability to hold personnel accountable to the process and continuously looks for ways to improve the process.
- **Defined Roles and Responsibilities** - Clearly defined roles and responsibilities should mandate personnel are to be trained on prior to process roll-out.
- **Performance Metrics** - Baseline (how are we doing today?), benchmark (how are others in the industry performing?) and goals (what level of performance do we want to demonstrate to be on par with the competition and on what areas of performance do we want to "beat" the competition?). Upon achieving performance goals determine when to "raise the bar".
- **Data Integrity** - Ensuring ownership of each element of customer data throughout the customer lifecycle.
- **Continuous Improvement** - The reality is that these processes are NEVER done. On a periodic basis (monthly or quarterly) stakeholders of each process should get together to discuss what is working, opportunities for improvement and make recommendations on changes to meet the ever-changing needs of the customer.

The benefits that you will realize from a focus on consistent and repeatable processes include increased customer and employee satisfaction, as well as improved operational efficiencies. Investing in this area allows you to respond to both the immediate (short-term cost reduction) requirements and long-term operational goals.

Focus on Product Quality Instead of New Features

To make the most of the current economic environment you are encouraged to take actions that will directly benefit your existing customers. While your customers may have been originally “sold” on your features and functions they now have significant experience with the performance of your products and services. To the extent that you are meeting or exceeding your customer’s expectations on feature, function, quality and reliability you have some of the key ingredients necessary to establish a loyal customer-base and run a highly efficient organization.

If, however, the products you provide the market-place have quality and reliability issues (i.e., hardware malfunctions, software bugs, etc.) then you not only have a customer satisfaction issue, but your operating costs are higher than they need to be.



Is the following scenario all too familiar to you? Your company releases a new product (or version of an existing product). New customers buy it and existing customers upgrade to it. There are flaws that “could have been” caught within an effective quality assurance test (or prevented further upstream). Customers call-in to report the problem (they aren’t sure if they have installed it properly, are using it right, or if there is a quality/reliability issue). Your front-line team troubleshoots the issue, reproduces the outcome experienced by the customer and determines that the customer has properly installed and is correctly using the product. The call-center hands the issue off to your Tier II organization. Tier II troubleshoots, reproduces the outcome and confirms that it is an Engineering issue. Tier II hands-off the issue to Engineering. Engineering must prioritize this problem report amongst others previously received and provide feedback to the call center to set customer expectations. This chain of events could take hours, days, weeks or months…

Back to the customer…Meanwhile, the customer cannot effectively perform their job, using your product. If the issue is causing significant impact and cannot be immediately resolved by Engineering the customer demands a work-around. This work-around could come in the form of identifying ways to accomplish the objective using an alternative function in your product, or it could require a temporary fix created by your Tier II or Engineering organization.
The impact of the above scenario includes, at a minimum:

- Customers becoming increasingly skeptical about your products and their satisfaction will decrease.
- Your call center, Tier II and Engineering teams spending time in “reactionary” mode, a highly inefficient way to use your resources.
- Your Engineering team being required to ensure that the “next” product release includes the temporary fix(es) that have been implemented ensuring subsequent releases don’t reintroduce the problem(s).

The adage “get it right the first time” is what this lesson is all about. If you should find yourself in this scenario you are encouraged to:

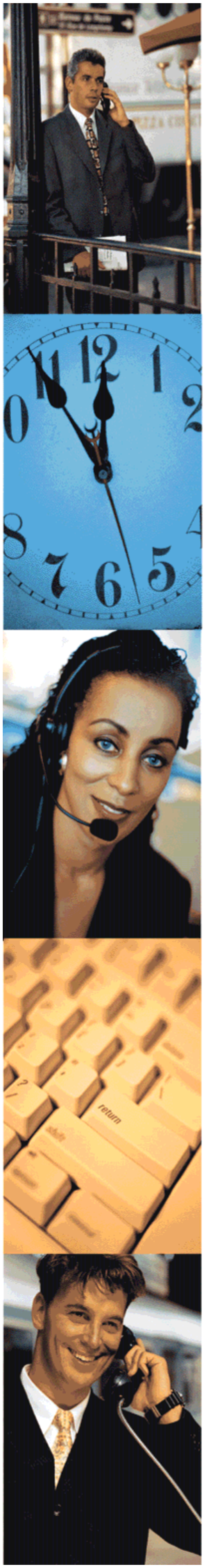
- Implement an effective quality assurance process and methodology through-out the product development lifecycle.
- Put significant focus (senior management attention) on “plowing through” outstanding quality and reliability issues.
- Let your customer-base know what you are doing, to set their expectations.
- Do what you said you will do.

The above steps “may” initially have to come at the cost of delays in releasing new features and functions. In many cases you will find that your customers would rather have what they’ve already purchased working properly than new features and functions.

If the products you provide the market-place have a high-degree of quality and reliability then not only will your customers be more satisfied, but your operating costs will be lower than they otherwise would be if you are “subsidizing” inefficiencies inherent in organizations delivering poor quality products. Make no mistake, where there is software (for example) there are bugs. However, the ratio of problem reports, due to malfunctions or bugs, should represent a very small percentage of the total number of inquiries your call center receives from the customer.

Enabling Customers to Self-Serve

When done properly, one of the most effective ways to increase customer satisfaction while reducing operating costs is that of empowering your customers to self-serve. Customers WANT to have more control, especially if it makes it easier to do business with you. Prior to embarking on this endeavor,



however, you are encouraged to make sure that you are not implementing technology in such a way that it becomes an obstacle to the customer getting the support they require. An example of “ineffective” technology (from the customer’s perspective) is that of a phone system with an elaborate “tree” of options.

Self-service capabilities are best received by the customer-base when made available as an option, and not forced down their throat. And, there should always be an “escape hatch” providing an option for the customer to work with a real-live human-being.

Key technologies that enable you to increase your customers’ ability to self-serve include your phone system and web-site. You can get started by simply making frequently asked questions (FAQs), about your products and services, available on your web-site. From there you can take steps to offer more sophisticated capabilities such as implementing a searchable knowledge base that allows the customer to ask a question (i.e., how do I…) and receive possible solutions (in ranked order) to address their question. A major consideration in implementing a knowledge base, however, is that it does NOT populate itself with useful information. You will need to assign an administrator that is responsible for obtaining common problems and solutions from your customer service system, and loading this information into your knowledge base in a standard and easily retrievable format.

To ease your customers into the online support option have your service personnel co-browse the FAQs or knowledge base with callers so that they become familiar with the content and methods of access.

In addition to having access to FAQs, and a searchable knowledge base, customers also find value in being able to:

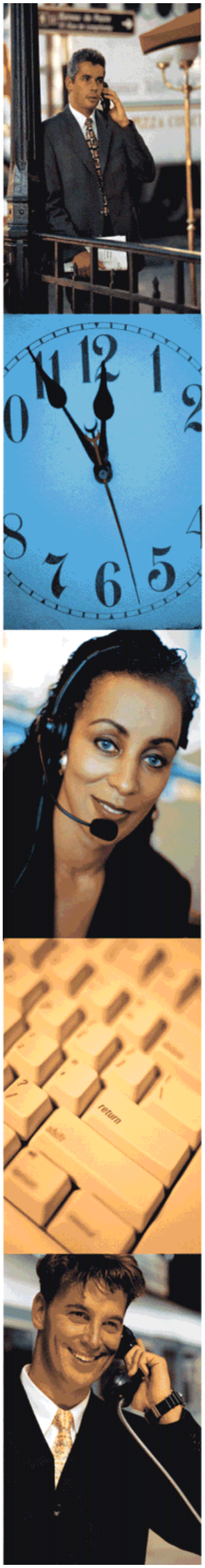
- Enter a problem report or question directly into the customer service system
- View status of reported problems or questions
- View and update profile information
- Place orders and track status
- View and pay invoices
- Request a password reset

To determine which of the above “transactions” would provide the most benefit (to your customer and your cost structure) you should perform an analysis to determine the most frequent and/or labor intensive interactions that you have with your customer-base. These should be targeted as opportunities to automate, enabling the customer to self-serve.

The final ingredients to obtain the maximum value (increased customer satisfaction and decreased operating costs) you are encouraged to include the following in your self-serve capabilities:

- Integration
- Motivation
- Security
- Follow-up

Integration: make sure that you capture data about the customer’s self-serve interaction and that your contact center has access to this information. For transactions where the customer is not required to identify themselves capture general data elements such as what they were viewing, which can be useful for future analysis. When they do identify themselves, capture the customer id, what they were viewing, and how the transaction was completed. By doing so you can pick up where the customer left off (as a continuous thread), if they are not able to get what they needed and decide to call or e-mail for help.



Motivation: offer customers something for using the self-serve option. An example includes putting them at the top of the queue if they end up having to call or e-mail for support, on an item that could not be completed online.

Security: ensure your self-serve site has appropriate security and privacy. Customers need to feel comfortable that no one else can see their information (problem reports, profiles, orders, invoices, etc.)

Follow up: at the end of each self-serve interaction BRIEFLY ask how it went, if they got what they were looking for, and if there is anything that could be improved.

While the above approaches to increase your customers' ability to self-serve are highly focused on technology, the final comment is that this is NOT a technical problem. Technology is merely the enabler. A major step you will need to take, prior to investing in and implementing technology, is that of ensuring your business processes are designed for data integrity and that the information generated is customer viewable. The last thing you want is someone placing inappropriate comments about a customer into a system and having it show up, online, for customer consumption.

Segmenting the Customer Base and Support Levels

Does your company treat all customers equally? Perhaps they are equal. However, many firms realize that their customers have diverse needs and expectations. If this is a reality for your firm, and you have not yet performed customer segmentation, you may be overlooking many opportunities to improve customer satisfaction AND reduce operating costs.

The primary reason to perform segmentation of your customer base is to tailor your complete customer relationship model (sales, marketing and service) to meet or exceed the expectations of customers with differing needs. Too often, companies look at ways to improve customer satisfaction and operational efficiencies "across the board" with a "one-size-fits-all" approach. This can be an inefficient application of a firm's precious resources.

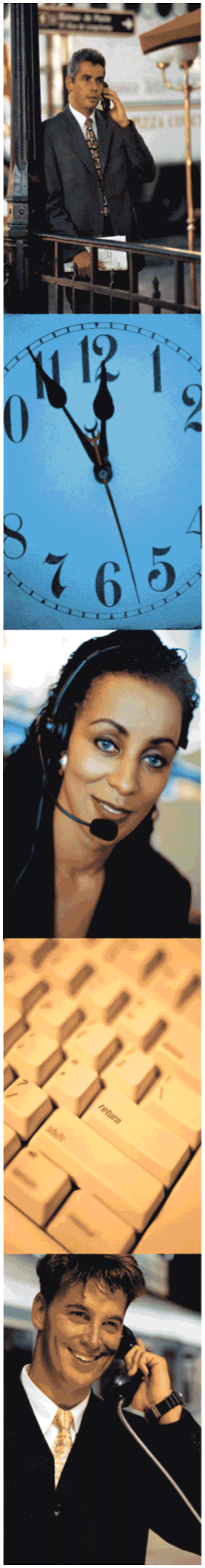
Companies can typically categorize their customers into at least 3 segments. For the purpose of this discussion we will generically label the segments as follows:

- High-End
- Medium
- Low-End

High-End – This segment contains those customers that are "more equal" than others. That is, these customers generate the most revenue for the firm, represent a strategic relationship and/or have the potential for significant growth in the future. This segment, representing only a small percentage of the entire customer base, likely requires a level of service that is high-touch, personalized and relationship oriented. These customers, more so than those in other segments, have "bet their business" on your products and services; they expect you to be a trusted advisor, partner or extension of their firm. These are the customers for whom you will want to continuously attempt to "exceed" expectations.

Low-End – These are customers that deal with your firm on a transactional basis. Typically, customers in this category merely want a low-cost and efficient transaction. To the extent that you can "meet" this requirement, these customers will remain loyal. However, as soon as another provider offers similar products and services for a better price, the customer will consider how they can switch, when their contract is up.

Medium – This segment may actually represent the largest (from a customer count perspective) of the 3 segments, containing customers that are at neither of the extremes (high or low-end). The needs of this segment can be the trickiest of all to address.



I have found that, in advance of segmentation, customer satisfaction scores could be predicted for each segment: Low-end customers would be highly-satisfied and require no additional attention (from a continuous improvement perspective). High-end customers would be "fairly" satisfied needing some additional attention. Medium segment customers would be the least satisfied and need the most attention of all.

In my experience, further analysis often revealed that, after several years of driving continuous improvement efforts directed at the entire customer-base, the low-end customers benefited the most from the one-size-fits-all approach, while most of the high-end customers were already recognized, with programs or senior account teams in place to cater to the needs of customers in this segment. However, it is the medium segment, containing customers just above the low-end, and just below the high-end, that is the least understood segment of all. If this (likely) scenario plays out for your firm, the next step to consider is that of slicing the medium segment into 2-3 logical segments.

Once you have placed your customers into the segments that make sense for your firm, you can consider how to deliver on the expectations of each. This includes how you will market, sell, and provide support to each segment. You might consider the following:

Leveraging partners / VARs to perform Sales and Support for a segment of the customer-base. Introducing new levels of support and charging appropriately, e.g., charge different fees for 1 hour, 4 hour, 8 hour response, or off-hours support. These must be offered as a new service, previously unavailable, rather than to begin charging for something that was previously free.

One of the most frequently expressed concerns of customers is that the firms they do business with seem to be disjointed, that each contact with the firm feels like a separate company. As such, a customer segmentation initiative should consider EVERY touch-point that the customer has with your firm. If cross-functional coordination doesn’t take place during your customer segmentation initiative, the result may be that you further exasperate this situation.

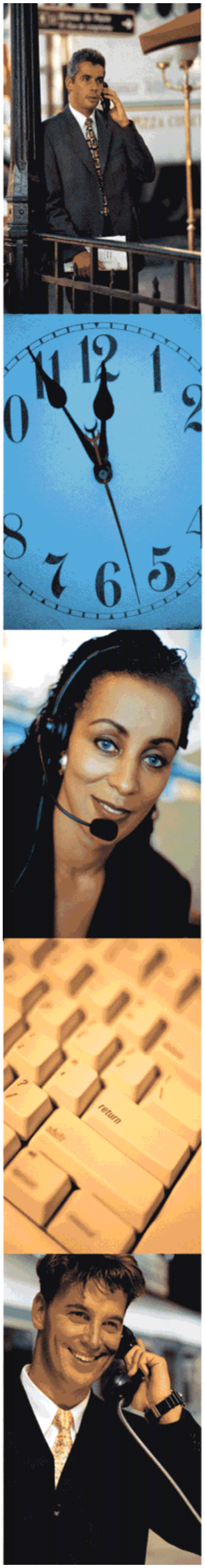
Segmenting your customer base into groups of customers with similar expectations and aligning your entire organization around the segmentation model will provide your firm with many opportunities to deliver the products and services to your customers more efficiently. Not only can this reduce the cost of service delivery, but it will also improve customer satisfaction and loyalty as you more effectively meet the needs of each customer.

Make Informed Decisions, Not Random Cuts

Make no mistake, cost cutting (including downsizing) is no simple matter. When it does come time to cut costs, you are encouraged to acknowledge the fact that not all organizations in your company deliver equal value to the customer. Ask yourself the question: "Who is paying my salary, and the salaries of my employees?" There is only one answer: the customer. In order to retain your existing customers, and revenue stream, you will want to minimize or eliminate the impact that cost cutting has on the customer base.

Too often, companies take what I call the "peanut butter" approach to cost cutting, by asking each organization to cut X% from their budget. That is, the cost cutting is spread equally across each functional organization. Requiring each organization to cut the same percentage of expenses from the budget is not getting at the root cause of the issue. In fact, you will often find that "fat remains" after taking such cost-cutting approaches. While costs are reduced, the fact is that there will still be "pet projects" or activities that continue to occur, consuming the valuable time of your corporate resources, even when they may not be aligned with the overall direction of the company.

The root cause of the issue is that expenses are out of line with revenue. The cost structure of the organization has grown over time to support new customers that bring new revenue. The fact remains that you have an existing customer base that is providing the base revenue that you enjoy today. Taking anything away from the existing customers, in the way of service, support, quality and responsiveness, will give your customers a reason to defect.



To identify the areas of your business that provide the most value to your bottom-line, you are encouraged first to quantify the impact that each organization and activity has on the customer, then to determine the return-on-investment that each provides. An effective way to approach this is from the customer's perspective, looking at your organization from the outside in. Which organizations "touch" customers most frequently? Which organizations do the front-line resources (Sales, Account Management and Service) depend on most to meet customer expectations? If cuts in these organizations are too deep or too random, customer service will be most severely impacted. Understanding your highest value activities allows you to know which areas you want to remain very strong in, and which areas can absorb the deepest cuts.

The final and most challenging step is that of redesigning the organization accordingly. To do this you are encouraged to pull your management team together in an environment of "we are starting a new business, from scratch." The major ground rule for this exercise is that no one at the company has a guaranteed job. Throw all the resources up in the air. In fact, some of these leaders may be "impacted" as a result of this exercise.

With your highest value activities identified, you can structure the organization from the bottom up to manage the business in the most cost effective way, while continuing to meet or exceed your customers' expectations. The focus here is on identifying the required resources and applying the best people to the truly valuable activities that your firm performs. The positive aspects of this exercise versus a "true" startup, are two-fold:

1. You have an existing customer-base that is asking you to serve them.
2. You have a pool of people that are ready to "get started NOW"…

While cost cutting may be inevitable, intelligently approaching this will help to ensure the long-term success of your enterprise.

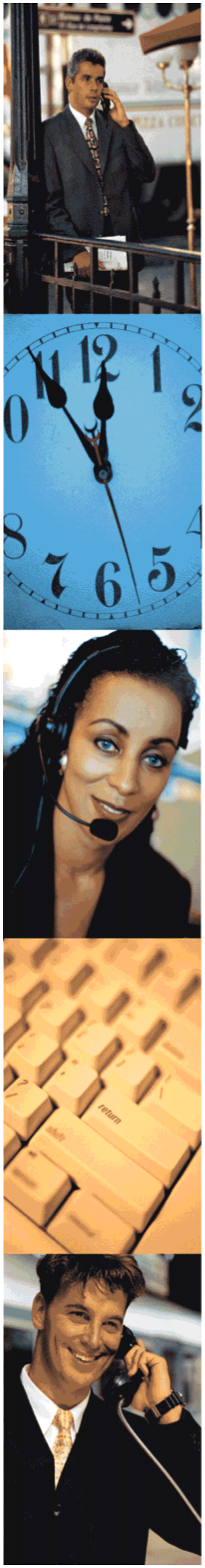
Cease Big, Expensive Projects with Long-Term ROI

For many years, companies were struggling to keep up with the fast pace of evolving technology. With pressures like quicker time to market, it was often easier to make quick system and process enhancements rather than invest in large system and process overhauls. However, good companies knew they had to start thinking about the long-term as well. To use an analogy: an old jeep can only be fixed so many times; eventually you need to invest in a new jeep.

Just when many companies felt caught-up enough to think about a longer time horizon, the bubble burst and the economy turned. The long-term picture is not as clear now, in many cases. The current pressure is to cut costs while maintaining customer satisfaction levels. Every dollar spent today needs to return more dollars sooner rather than later, which means short-term ROI. Multi-million dollar projects with delayed payback need to be deferred. The old jeep needs to last a little longer before being replaced.

A common theme throughout this newsletter series on cost cutting is identifying a company's priorities. While long-term priorities are important and should not be overlooked, the immediate concern is the short-term. Companies should make short-term investments that are in line with their priorities and will enable them to "hit the ground running" with larger investments for the long-term when the economy stabilizes. Often this means continuing to use existing systems, while perhaps enhancing processes or providing additional training to personnel.

The long-term is important and should always be a consideration in decision-making. However, in this economy, it is important to make the right investment decisions in the near term to make sure the company will survive for the long run.



Renegotiate Vendor Contracts

Just as you are trying to retain your customers by keeping them happy, so are your suppliers. In cases where you have flexibility in choosing vendors, you have an opportunity to increase the value received for the price of the products and services that you buy. This could include at least 3 negotiating points with your supplier:

1. Cost reduction
2. Increased level of service for the existing price
3. Lower minimum purchase agreements

Cost Reduction

Price is a key factor affecting customer satisfaction and retention in the current business environment. If switching vendors for a particular product or service is an easy option for your company, let your suppliers know price is a deal breaker in your relationship. Companies eager to keep your business will be willing to negotiate. If not, find another vendor who is eager to obtain your business at a lower price. However, it is important to keep in mind some important points when considering alternative vendors:

- Price is an important consideration, but not the only one. You should be careful not to compromise quality or other important factors.
- Many companies are having their own difficult times. Be sure you assess the financial stability of a company before relying on them for any significant part of your business.

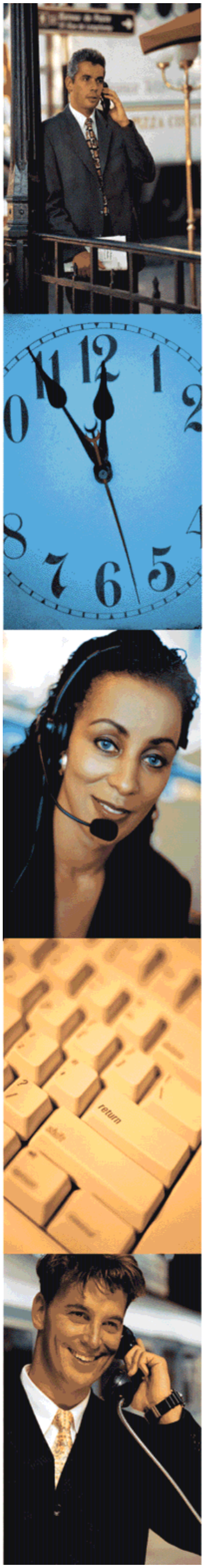
Increased Level of Service for the Existing Price

While a vendor might not be able to renegotiate price in this economic climate, you might be able to get other things of value to you, such as an increase in the level of service that they provide your firm, within the existing pricing structure. This could include increased responsiveness and/or additional flexibility in the services that they render to you. Additionally, you should tie financial penalties to their performance (if you haven't done so already). And, when they don't perform to the standards that you have agreed to contractually, you have lowered your costs or increased the value of something else that you can get from the vendor. Obviously, you don't prefer "less than adequate" service to obtain a discount, but tying performance to cost is one way to ensure that your supplier performs to the levels that you expect (or better).

Lower Minimum Purchase Agreements

If you are still living with contracts that were negotiated during the boom, you may have agreed to higher than presently required volumes, as a minimum purchase agreement. You should review your current volume requirements and where they fall significantly below the minimums in your contract, work with your supplier to bring the two in line. You might also consider negotiating more favorable purchasing timelines.

In general, the more a company relies on your business, the more leverage you have to renegotiate contracts and increase the value received for the price. With a more stream-lined cost structure, your company is in good shape to maintain or increase customer satisfaction while reducing operating costs, thereby avoiding the "death spiral."



More About Customer Centricity, Inc.

Customer Centricity, Inc., is a business consulting firm that works with companies to align their resources to exceed customer expectations in the most efficient and effective manner possible. We leverage our real-world experience to help our clients continuously improve their service delivery and management capabilities to:

- Increase profitability
- Improve customer satisfaction and retention
- Increase operational efficiencies
- Improve employee satisfaction

Customer Centricity optimizes the interaction between people, process and technology in several ways:

- Comprehensive assessment methodology to identify the actions that will yield our clients the greatest return
- Skills Training to enable customer-facing personnel to deliver exceptional levels of customer service
- Design and Implementation of business processes to serve the customer and manage corporate resources in efficient, effective and consistent manners
- Identification of the appropriate business processes to automate, enabling companies to get the most from their investments in technology

Customer Centricity's approach is to work closely with our clients to help them understand what they are doing right, and their opportunities for improvement. We provide pragmatic recommendations that provide immediate benefits, and we drive continuous improvement programs help our clients realize significant return on investment in a very short period of time (measured in weeks, not months or years).

To learn more about Customer Centricity, call 603/491-7948 or visit our web-site, www.customercentricity.biz