



# CFO Forum: Protecting your bottom line





# Introductions



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# Why Margin Protection is a hot topic

**BBC NEWS** Brexit: New era for UK as it completes separation from European Union

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**The Guardian** News website of the year  
Energy industry  
West feeling impact of Russia sanctions too as oil and gas prices soar

Mon 7 May 2022 17:47 GMT

Larry Elliott

**Internet Retailing**

A quarter of UK retailers say they are four weeks away from going bust due to supply chain crisis

INDUSTRY 22 Jun 2022 by Paul Skeldon

**CNBC**  
MARKETS BUSINESS INVESTING TECH POLITICS CNBC TV  
EUROPE NEWS  
UK energy bills to rise by 80% in October as regulator announces hike

**FINANCIAL TIMES**

UK inflation

IMF warns high inflation will persist longer in UK than similar economies

Kwarteng's unfunded tax cuts criticised as chancellor prepares

Source:

"Brexit: New era for UK as it completes separation from European Union," BBC News, January 2021

"West feeling impact of Russia sanctions too as oil and gas prices soar," The Guardian, March 2022

"A quarter of UK retailers say they are four weeks away from going bust due to supply chain crisis," Internet Retailing, June 2022

"UK energy bills to rise by 80% in October as regulator announces hike," CNBC, August 2022

"IMF warns high inflation will persist longer in UK than similar economies," Financial Times, October 2022



# What do we see businesses doing?

## An Illustrative Profit and Loss Statement

£'000	FY23
Revenue	X
Direct Costs	(X)
<b>Gross Profit</b>	<b>X</b>
Production Overheads	(X)
<b>Operating Profit</b>	<b>X</b>
Indirect Costs	(X)
<b>Profit / (Loss)</b>	<b>X</b>



# What do we see businesses doing?

Businesses prioritise revenue and focus on passing the costs to the customers

An Illustrative Profit and Loss Statement

£'000	FY23
Revenue	X
Direct Costs	(X)
Gross Profit	X
Production Overheads	(X)
Operating Profit	X
Indirect Costs	(X)
Profit / [Loss]	X

- When it comes to Margin Protection, businesses often focus on revenue as a proxy for profit
- However, many do not:
  - Pass on all cost
  - Refresh the price list to reflect the changing market and economy
  - Review the pricing/quotation methodologies and avoid revenue leakage



# What do we see businesses doing?

Businesses address each cost bucket in isolation starting with 'easier' costs and avoiding difficult, longer term decisions

An Illustrative Profit and Loss Statement

£'000	FY23
Revenue	X
<b>Direct Costs</b>	<b>(X)</b>
Gross Profit	X
<b>Production Overheads</b>	<b>(X)</b>
Operating Profit	X
<b>Indirect Costs</b>	<b>(X)</b>
Profit / (Loss)	X

- Businesses often tackle costs in a 'horizontal' manner by taking an individual cost bucket and remove the "easy wins"
- However, many do not:
  - Look past easy wins and the 'safer option'
  - Understand which costs contribute to the bottom-line (value adding activities) and which do not
  - Make difficult decisions to align the costs base to the future direction of the market



# What is another way of looking at it?

Break down the P&L into meaningful sub-P&Ls as informed by the cost drivers

## An Illustrative Profit and Loss Statement

£'000	Sales Channel A	Sales Channel B	Sales Channel C
Revenue	X	X	X
Direct Costs	(X)	(X)	(X)
<b>Gross Profit / (Loss)</b>	<b>X</b>	<b>X</b>	<b>(X)</b>
Production Overheads	(X)	(X)	(X)
<b>Operating Profit / (Loss)</b>	<b>X</b>	<b>X</b>	<b>(X)</b>
Indirect Costs	(X)	(X)	(X)
<b>Profit / (Loss)</b>	<b>X</b>	<b>X</b>	<b>(X)</b>

- There is no 'one size fits all'. Each business will have its own cost drivers
- A couple of examples include: by product, by customer, by division, by sale channel, by process and by facility
- Many businesses have developed traditional ways to cut their cost base, often limited by their finance systems or organisation structures



# What is another way of looking at it?

Prioritise costs which do not contribute to a value adding activity

## An Illustrative Profit and Loss Statement

£'000	Product A	Product B	Product C
Revenue	X	X	X
Direct Costs	(X)	(X)	(X)
Gross Profit / (Loss)	(X)	X	X
Production Overheads	(X)	(X)	(X)
Operating Profit / (Loss)	(X)	X	X
Indirect Costs	(X)	(X)	(X)
Profit / (Loss)	(X)	X	X

- Cutting the cost data in many ways (horizontal and vertical) creates additional insight on margins
- For example, one product could be off-setting the margin of all other profitable products when all costs are allocated
- This signals that costs attributable to this product contribute to a non-value adding activity and hence could be optimised / removed
- You can also create scenarios to make informed decisions for the future

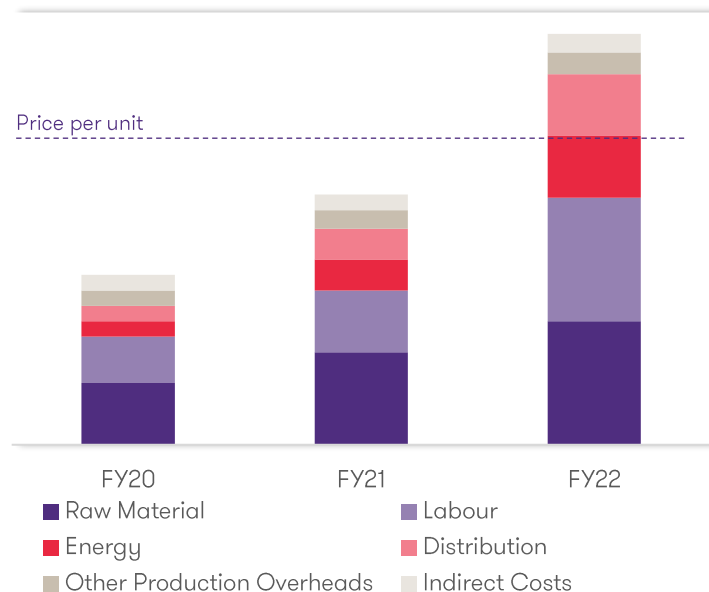




# What is another way of looking at it?

Use detailed cost analysis to inform your pricing strategies

## An Illustrative Cost Stack for Product A



- Detailed cost allocation and cost analysis could be used to inform price negotiations or to revise price lists (avoiding any revenue leakage)
- In B2B, it is also helpful to demonstrate to your customers that costs are being optimised before asking for increases



# To conclude

There is no 'one size fits all'

## 1

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You can grow your margin by maximising revenues

*Or you can analyse and optimise your cost base and use this information to inform your profit focused strategy*

## 2

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You can analyse each cost bucket separately to identify isolated cost reduction opportunities

*Or you can analyse your costs in a vertical and horizontal manner to identify and optimise the costs associated with non value adding activities*

## 3

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You can identify and reduce some costs without making strategic decisions

*Or you can comprehensively analyse costs to create scenarios and make bold decisions more safely*



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