

Root Cost Analysis:

Innovative cost improvements in IT



Catalyst: helping you to significantly enhance the return on your technology assets.

If you'd like to hear more, contact us on: +44 (0)870 901 4155.

In today's challenging environment, technology departments are in danger of being crushed between the pincers of growing business expectation, and an unstinting focus on cost control.

Identifying further sources of cost reduction in your technology assets is akin to drilling for oil in a depleted well. Savings get harder and harder to find.

Catalyst has developed a technique for drilling into previously undiscovered areas of inefficiency and waste, and then rigorously eliminating them. We call our methodology Root Cost Analysis.

The story doesn't end there – applying Root Cost Analysis creates a platform for the re-engineering of your technology assets for faster and more effective business management and growth.



A relentless focus on costs

With almost relentless pressure to reduce expenditure, banks are once again turning to technology departments for further cost reductions. However CIOs know that, like an oilfield that has been largely depleted of reserves, the usual sources of cost savings have little left to yield. The obvious routes – headcount reductions, offshoring, tighter vendor management – have generally been pursued to the point of exhaustion.

Time for a new approach?

Catalyst has an approach that is radically different. An approach that is as compelling as it is comprehensive. An approach that is necessary because business expectation is continuing to rise – and scaling back on the services the technology organisation provides is simply not an option.

The graph below demonstrates the growing disparity between what the business needs from technology to sustain competitiveness, and the capability of IT departments to deliver it.

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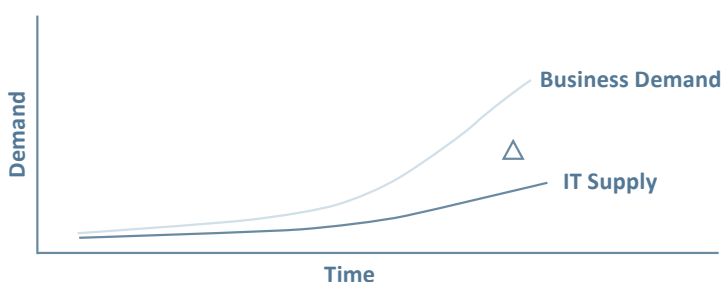


Fig 1. The growing gap between business demand and technology's ability to deliver.



Catalyst has identified several reasons for this generic situation:

- Technology is increasingly at the centre of the business – it now delivers substantial revenue streams, and is no longer just a ‘service’;
- Growing product complexity, and the need to commoditise these products quickly to reduce costs;
- Major regulatory changes, globalisation, legacy constraints and fundamental changes in the market landscape, which are all creating an overlay of additional complexity.

The challenge facing CIOs is not simply driving out inefficiency and cost – it’s about how to deliver more for less.

The roots of the problem

Typically, efficiency initiatives in the realm of technology struggle for two major reasons: organisation structures and poor financial reporting.

Looking at the first of these: technology departments in many capital markets firms tend to have similar structures; with vertically organised and business-aligned application teams, and horizontally oriented enterprise-wide services.

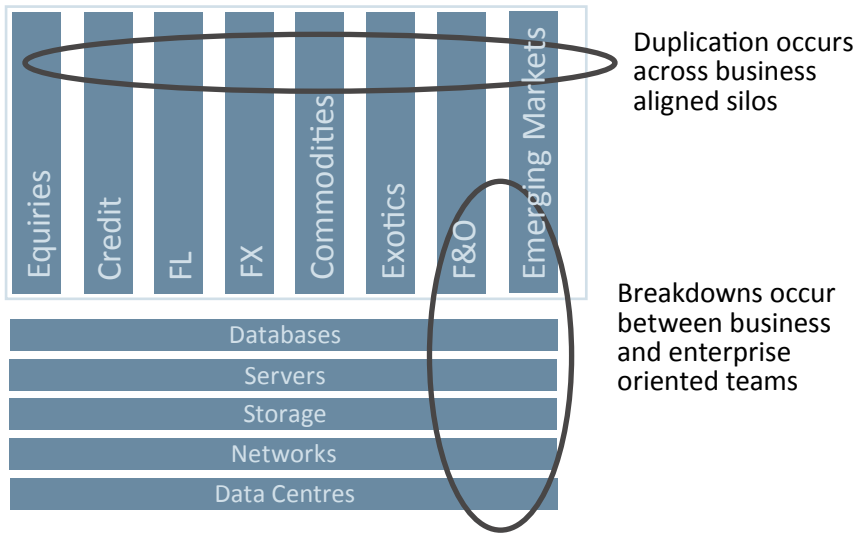


Fig. 2 Typical Financial Markets organisational structure, illustrating potential sources of inefficiency

Managers of these vertical and horizontal groups form the bedrock of the CIO’s management team, but these individuals tend not to focus on efficiency measures holistically – hence initiatives are generally implemented within these silos, rather than across them. As the diagram above demonstrates, this can result in large swathes of duplication and inefficiency persisting even after conventional cost reduction exercises.

Turning to financial information: when CIOs look to identify inefficiencies they frequently rely either on internally generated management reports, or on anecdotal opinions, to gauge performance. Neither source is reliable – financial reporting loses value for cost management decision-making because the information is distorted or diluted as it filters through the organisation. In addition, cost allocation methodologies and pooling mechanisms often obscure critical detail.

Driving sustained improvement

Catalyst has developed a unique approach to addressing these problems. Root Cost Analysis allows us to identify unnecessary cost in areas that are generally not visible at the level of CIO. To return to the analogy of an oilfield – with a little further ‘exploration’ – Catalyst can both identify untapped reservoirs of inefficiency, and reposition and reengineer IT assets to support the growing demands of the businesses that technology serves.

Hence Catalyst’s approach goes beyond merely identifying new sources of inefficiency, which like pockets of oil, will also in time run dry. It is more akin to developing renewable sources of energy – applying our methodology effectively engineers cost and waste out of the system for good – improving long-term competitiveness as a result.

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Case Study

Mining for hidden savings at a major European bank

We worked with the capital markets division of a Tier 1 capital-markets bank, deploying Root Cost Analysis to examine two discrete and major application environments.

Our methodology

We used our unique four-step methodology to identify the real cost of supporting these applications, as against the data provided by two conventional methodologies: cost centre reporting and a technology timesheet system. These steps were:

1. Selection of two sample applications for analysis.
2. Collation of existing data reports.
3. Drill down into reports and processes.
4. Critical questions and identification of potential savings.

What we found

To the surprise of our client, we ascertained that the total cost of application ownership, as revealed by the drill-down sample, was several times greater than was implied by either of the client's own financial reports.

Cost as per:	App. 1	App. 2
Client's Cost Centre Report	€2.5m	€6.2m
Technology Timesheet system	€3.9m	€5.1m
Root Cost Analysis	€9.4m	€10.7m

What we delivered

As a result of applying Root Cost Analysis, we identified 30 specific recommendations that were not apparent at the outset of the study. In fact, Catalyst's analysis potentially paid for itself by identifying possible savings from market data charges for the applications-development teams.

We delivered recommendations with significant cost-saving potential in four specific areas:

- **Pooled System Administration (SA) and Database Administration (DBA) costs:** to refocus away from activities with low business value-add, reducing cost and opening capacity for business growth;
- **Pooled network charges:** where little accountability had existed for network optimisation;
- **Accountability for application costs:** where no one individual had been accountable for overall application costs;
- **Control over investment and cost decisions:** where we were able to challenge the focus on developer headcount, which in practice represented only 17% of TCO.

Taken in total, the recommendations developed by applying Root Cost Analysis delivered the client not only opportunities for substantial cost savings, but also the prospect of meaningful and sustainable improvements in efficiency through:

- The transfer of expertise and resources from low to high value adding activities, resulting in the faster delivery of new business functionality;
- Freeing up capacity, enabling faster business growth, quickly and at no incremental cost;
- Avoiding further cost cutting in important business activities.

Identifying untapped sources of inefficiency: the Catalyst approach

At the outset, we comprehensively assemble financial information that is not generally available to CIOs, and analyse the data forensically to deliver clear and comprehensive visibility of inefficiencies that exist within vertical, business aligned technology silos.

Our methodology has parallels in the way petroleum geologists take core-samples, by drilling vertically within single lines of business and going deep into them, continuing down into the enterprise services that support them to identify duplication and inefficiency. As a result, we can identify potential cost savings across the entire technology organisation that cannot be realised within any one of the vertical silos alone.

“The output of Root Cost Analysis will include more than cost reduction”

Root Cost Analysis: what we do

Root Cost Analysis is unique in our industry. It requires specialised skills, knowledge of what to look for, and experience of identifying otherwise invisible inefficiencies and superfluous costs.

In practice, applying the principles of Root Cost Analysis has four key stages:

1. Current data sources and reports are collated and reviewed.
2. The costs associated with the given services are drilled into, examined forensically, and thoroughly tested for value contribution.
3. Value contribution is comprehensively assessed within a tightly defined business context.
4. Opportunities for reducing or eliminating inefficiency are identified, and recommendations formulated accordingly.

Delivering multiple benefits

Catalyst’s methodology delivers unparalleled visibility of inefficiency inside the vertical (that is, business applications) silos and the horizontal (that is enterprise services) that support the business line.

Informed by this clarity of vision, we make client recommendations at several levels:

- Quick Wins: for example, the elimination of redundant testing capacity. Often cost savings from Quick Wins alone can exceed the cost of the initial consultancy exercise.
- Quantified medium term savings: recommendations around detailed cost saving action plans – for example, in areas of process automation.
- Strategic recommendations: identifying areas that will benefit significantly in the longer term through re-engineering core activities. Examples include the elimination of redundant func-

tionality or retiring of legacy systems.

- The clear identification of previously hidden operational risks, exposed by our thorough examination of internal processes: for example, where an overreliance on manual procedures increases the risk of systems failure.
- Reconfiguration: Root Cost Analysis is designed not just to identify inefficiencies, but also to engineer them out of the client organisation. By using technical, business, process and organisational skills, Catalyst looks at the problem space from a cost and an efficiency perspective.

The output of Root Cost Analysis will include more than cost reduction – it will also deliver significant and sustainable improvements in efficiency and risk control, and more focused client service.

If you'd like to know more about how we can help you improve the performance of your technology assets, please contact us.

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