

## **EFFECTS OF A SHARED SERVICES STRATEGY ON COST REDUCTION: A CASE STUDY OF EAST AFRICAN BREWERIES LIMITED**

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### **ABSTRACT**

Moving to a shared service method of operation entails a huge culture change for an organization. The entire business context must be changed. It takes time, effort and vast amounts of management energy to move from a mindset of purely decentralized management of support activities within each business unit or centralized management of support activities at the corporate level to a mindset of partnership between business units and the consolidated, shared service organization. Together with this, shared service units, despite their importance, receive much less senior executive attention than business units in most companies. The logic for this is that business divisions generate profits, and that is where top management often focuses its time. There is therefore a risk that an organization can lose its focus on shared services if the method is not shown to result in tangible benefits.

The objectives of the study were to establish whether there has been a reduction of transactional costs at EABL as a result of moving to a shared service environment; determine the extent to which the shared service strategy resulted in reduction in employee headcount and overheads; find out how shared service strategy led to improvement in inventory management; and establish how shared service strategy at East African Breweries Ltd has impacted on procurement costs.

The study employed the case study design, targeting all the departmental heads working at EABL's shared services centre. Purposive sampling was used to select 10 respondents, among them nine departmental heads from Information Technology (IT), finance, procurement, Human Resource, EABL Kenya Demand, EABL Kenya Supply, CGI, East Africa Malt Ltd, and UDV; and one top management representative. Data was collected from the participants using a semi-structured questionnaire and an interview schedule. Qualitative and quantitative techniques were

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employed in data analysis. Qualitative techniques involved giving a detailed account of the impact of moving to a shared services strategy on EABL's cost reduction efforts. Quantitative data was analyzed using descriptive statistics including percentages and frequency counts.

The study established that moving to a shared services environment has led to significant cost reduction efforts of East African Breweries Limited. Shared services led to reduction in procurement costs, reduction in employee headcount and overheads, improvement in inventory management, and reduction of transactional costs. As such, companies running their different functions as disparate competing entities should be encouraged to adopt shared services strategy to cut costs and operate more efficiently.

## **INTRODUCTION AND BACKGROUND**

As competition in the world of business increases, and demand for quality products and services from a more informed clientele rises, businesses are moving at a frantic pace to develop and capitalize on the competitive advantage that sets them apart from the competition. Additionally, companies have stepped up their globalization efforts to take advantage of opportunities in emerging markets throughout the world. As a result, we have seen a rush of mergers, acquisitions, and divestitures, as well as downsizing, rightsizing, and restructuring, all in an effort to position businesses to leverage their competitive advantage and build greater shareholder value (Forst, 2001).

Strategic positioning in a competitive environment is of paramount importance. In order to maintain a competitive advantage while embracing growth and expansion, organizations need to contain costs while maintaining best practice and world-class standards and processes. When championing penetration into geographically dispersed new markets, the need to ensure that best practice processes and standards are in place and continually improved becomes a basic survival tool for rapidly growing organizations (Porter, 1985).

One of the ways companies are looking for competitive advantage in this frenetic environment is through the reengineering or redesign of their core business processes, the end-to-end processes that touch customers and through which a company can make strategic changes. Another way is through the use of a tactical technique called shared services. In a shared service environment, a company pulls activities that support core business processes out of each business unit and

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consolidates them into a separate operating unit that runs these supporting processes as its core business process (Schulman et al., 1999).

Organizations and industries all over the world are under pressure to make business processes more efficient, eliminate unnecessary administrative support activity cost, and to banish duplication of effort and resources (Van Denburg & Cagna, 2000). Porter (1985) also identified support service as an area in the organizational structure where a competitive advantage may be gained by stating that the ability to share activities is a potent basis for corporate strategy because sharing enhances comprehensive advantages by lowering differentiation costs.

### **Statement of the Problem**

Moving to a shared service method of operation entails a huge culture change for an organization. The entire business context must be changed. It takes time, effort and vast amounts of management energy to move from a mindset of purely decentralized management of support activities within each business unit or centralized management of support activities at the corporate level to a mindset of partnership between business units and the consolidated, shared service organization. Together with this, shared service units, despite their importance, receive much less senior executive attention than business units in most companies. The logic for this is that business divisions generate profits, and that is where top management often focuses its time. There is therefore a risk that an organization can lose its focus on shared services if the method is not shown to result in tangible benefits. EABL moved to a shared services environment in 2001 but no studies have been conducted to show whether this has in any way contributed to the growth of the organization. Kirui (2001) conducted a study on competitive advantage through outsourcing of Non –core logistics activities within the supply chain of British American Tobacco Kenya. No study had, to the best knowledge of the researcher, been undertaken on the extent to which sharing of noncore services impacts on cost control efforts of corporate entities, this study will address itself to this problem.

### **Main objective of the Study**

The purpose of the study was to establish the extent to which shared services strategy affect Cost reduction efforts of East African Breweries Limited.

## **Specific Objectives**

The specific objectives of the study were:

- i. Establish whether there been a reduction of transactional costs at EABL as a result of moving to a shared service environment.
- ii. Determine the extent to which the shared service strategy resulted in reduction in employee headcount and overheads.
- iii. Find out whether shared service strategy improved inventory management.
- iv. Establish how shared service strategy at EABL has impacted on procurement costs.

## **LITERATURE REVIEW**

### **The concept of shared Services**

Shared services is a collaborative strategy whereby the staff functions of a firm are concentrated in a semi-autonomous organization and managed like a business unit competing in the open market to promote greater efficiency, value generation and improved service for internal customers. This strategy facilitates organizational flexibility and horizontal integration with good vertical control. Cost reduction, better service, best practices in delivering internal services to users are some positive outcomes of this application, as internal services now need to be delivered with a service-oriented approach to all users within the firm (Rao, 2006).

For most firms, switching to a shared services model inadvertently involves layoffs and major workforce restructuring. Further, new levels and kinds of cooperation are needed. All members of the new shared services unit are expected to interact and be interactive. This naturally requires new skills and demands from employees (Victor and Stephens, 1994). Having common business processes and common IT applications are important to justify the migration to a shared services model.

Schulman et al. (1999) suggest that three important levels of change are needed for this migration: defining responsibilities, that is, governance, accountability and measures to create accountability; focusing on efficiency, that is, processes, systems and economies of scale; and focusing on effectiveness, that is, skills, delivery system and organization. To develop the shared services organization in a phased manner, firms should gradually shift from being the service provider to being customer driven, and finally to being the business partner leveraging on the

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success achieved at each phase. The primary focus of shared services has been the concentration of transaction- orientated services that are repetitive and are much the same for each business unit. Generally, the types of services included in a shared services model include financial services including accounts payable and accounts receivable; procurement; human resources including payroll; property and facilities management; and information technology operations.

### **Theoretical models of shared service strategy**

According to Schulman et al. (1999) the decision to create a shared services business environment is a strategic decision and should be undertaken as a part of an organization's overall strategic vision. A shared service per se is "tactical" (Schulman *et al.*, 1999), and in this way the operations of a shared services provides a key factor in the organization ability to reach its strategic goals. Quinn, et al. (2000) identified four models that can be used to explain where an organization is in the journey towards shared services. These are, the basic model, the market place model, the advanced marketplace model, and the independent business model. According to the basic model the move to shared services involves the consolidation of transactional processing and administrative work. At this point the predominant drivers are cost reduction through economies of scale, standardization of processes, and a focus on customer service. The basic transactional model is also a mandatory service as all business units and companies must use this service within an organization, and are not allowed to go outside and source that particular service. Moving to a basic model creates value at two levels. First, operating costs are lower with a positive effect on the bottom line. Secondly, corporate functions and business units reduce human resources at transactional level, which can be re-positioned at tactical and strategic level (Quinn *et al.*, 2000).

The marketplace model is the next step in the shared services journey. The difference between the marketplace model and the basic model is the inclusion of professional and advisory services, as well as the separation of governance related activities. The professional and advisory services operate on a principle of an internal consulting service. According to Quinn *et al.* (2000) the separation of governance activities from the delivery of services is "the move to a real internal marketplace". The advanced marketplace model takes the total service approach further by bundling functional competencies (human resources, finance, information technology) with cross-functional synergies (people, knowledge, systems) to create a total service solution. This

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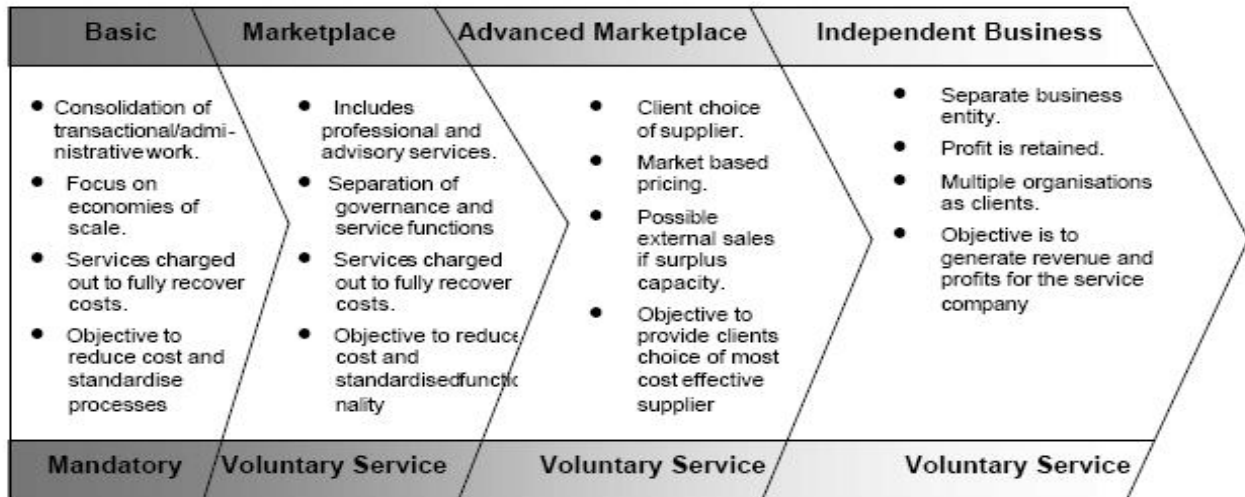
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total service solution also implies that the shared services business unit is not protected and the internal customer can purchase the service from outside. In the advanced marketplace model pricing is based on market prices. The shared services business unit must compete for the internal customers business, not only on pricing but also on offering, efficiency and effectiveness. In the basic and marketplace models, the shared services business unit is protected from outside competitors as business units are prohibited from using outside service providers for a period of up to two years. This is to give the business unit time to establish itself. During this period senior management can see if the shared services business unit supports the overall business strategy, or if it should be outsourced (Van denburgh & Cagna, 2000).

In the advanced marketplace model the shared services product offering can respond to changing market and customer needs quickly and efficiently, due to flexibility. In the advanced marketplace model the shared services move into the realm of supporting the organization's vision by being supplier of choice, and by supporting cross functional strategies. Performance measures should focus on achieving the organization's vision, market based pricing and possible external sales of the function and related activities. The Independent Business Model occurs when shared services operate as a separate business entity and becomes a profit center serving both internal customers as clients, and external customers. Few shared service business units are in this stage of independent business units. According to Gunn et Al. (1993), only 17% of today's shared services are separate legal entities. They are also of the opinion that "commercializing" the shared services business unit will lead to a higher performance of the shared services business unit (Gunn Partners, 2001). Figure 2.1 presents a summary of the four models of shared services.

**Figure 2.1: The four shared services models**



Source: Adapted from Quinn *et al.* (2000:36)

### **Benefits Attributed to a Shared Services Model**

Organizations that have implemented shared services are constantly reaping benefits that go beyond cost cutting and head count. These benefits are both tangible and intangible in nature. Tangible benefits includes; Cost savings through shared services centers can be in the order of 30%, sometimes more (Lester, 2001). According to Van der Linde (2002) cost savings is the major reason for implementing shared services. However, cost savings must go together with an increase in performance, effectiveness and efficiency (Quinn *et al.*, 2000). Working capital improvement gained from standardizing, concentrating and netting treasury activities, operating receivables, payables, and inventory management in a centre of excellence. This creates economies of scale, improves control and decreases expenses. Increased productivity which is achieved through (Forst, 2001). Enhanced professional services, shared services business units liberate governance functions from transactional functions, as well as professional staff from transactional processes to offering professional service (Quinn *et al.*, 2000).

Through process re-engineering, benchmarking and the use of best practices, cost savings are achieved that add value to the organization. According to Schulman *et al.* (1999) economies of

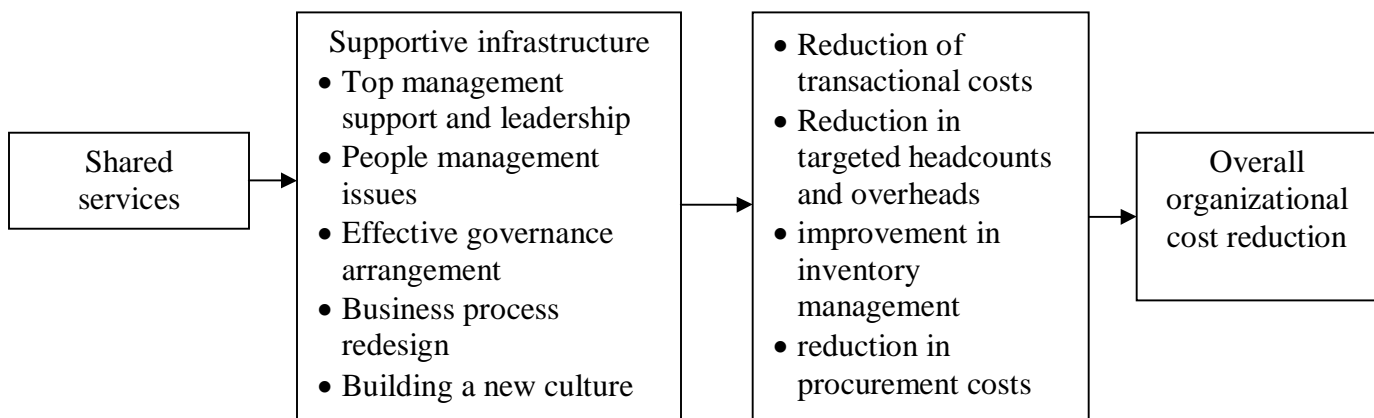
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scale are achieved through the standardization of processes that are experienced by customers Quinn et al. (2000) are of the opinion that because shared services rely on a team principle and the empowerment of employees to take decisions, it creates motivated teams that provide a consistent reliable cost effective service. Technology as well as qualified and multilingual staff enables a shared services business unit to conduct relationships with local, regional and global entities such as banks, governments and suppliers (Shah, 1998). According to Schulman et al (1999), shared services create one company approach where members of one organization the organization as a single entity. According to Uhlrich (1995) employees still have a boundary mindset about functions and functionality; shared services remove these boundaries by creating a common goal from doing a “job” to “add value”. Members in a shared services team share expertise (knowledge management), solve problems and add value through process re-engineering. This enhances team knowledge and according to Uhlrich (1995) it creates a new set of competencies and roles within the organization.

### Conceptual Framework

The figure 2.2 below presents the conceptual framework of the study.

**Figure 2.2: Conceptual framework**



**Source:** Researcher (2008)

Independent variables

Dependent variables

The study will find out whether shared services strategy, and existence of supportive infrastructure for success and growth of the shared services centre (the independent variables), have had an impact on cost reduction efforts of East African Breweries in terms of reduction of



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transactional costs, reduction in targeted headcounts and overheads, improvement in inventory management, and reduction in procurement costs (the dependent variable

## **RESEARCH METHODOLOGY**

### **Research Design**

The study was a case study of the effects of the extent to which a shared services strategy has affected the cost reduction efforts of East African Breweries Limited. According to Gay (1992), a case study is a research approach in which one or a few instances of a phenomenon are studied in depth. The main advantage of a case study is that it enables researchers to study a given case in depth. Since the interest of this study was to understand the benefits of shared services on one organization, case study was considered the best approach.

### **The Population of the study and data collection methods**

The target population of study was all the functional heads of departments working at EABL's Shared Service Centre and the MDs of the Kenyan based companies; viz KBL(2), UDV, CGI EAML. The organization has a total of 798 employees. Being a case study, the study involved functional heads of the following departments, which are represented in the Shared Services Centre: procurement, IT, finance, HR and MDs of the Kenyan based companies. As such, nine respondents will be selected. The study used both primary and secondary data. Primary data was collected from the respondents using a semi-structured questionnaire designed by the researcher. This was a questionnaire consisting of both open-ended and closed questions. It provides greater depth than is possible with a totally structured questionnaire. Secondary data sources included reports such as the financial reports and cost report from EABL. An interview guide was used to collect in-depth information from the top management on the impact of Shared services on cost reduction..

To ensure reliability and validity before the actual data collection, piloting or testing of questionnaires was conducted among five employees of EABL's shared services centre, who were not selected to participate in the actual study. The pilot study helped to improve face validity of the instruments. According to Chaves (1996), content validity of an instrument is improved through expert judgment.

## Data Analysis Methods

Since qualitative and quantitative data was obtained, both qualitative and quantitative data analysis techniques were employed. Qualitative techniques involved giving a detailed account of the effects that moving to a shared services strategy has had for EABL's Cost reduction. Quantitative data was analyzed using descriptive statistics including percentages and frequency counts. The results of data analysis were presented in frequency tables.

## DATA ANALYSIS, FINDINGS AND PRESENTATION

### Effects of Shared Services on Transactional Costs

The first objective of the study was to establish whether there had been a reduction of transactional costs at EABL as a result of moving to a shared service environment.

The nine heads of departments were asked to rate the impact of moving to a shared services strategy on transactional processing on a four point scale ranging from excellent to poor. Their responses are captured in Figure 4.1, which shows that 22.2% of the departmental heads rated transactional processing to be excellent, while 77.8% rated transactional processing to be good.

**Figure 4.1: Ratings of transactional processing after moving to SSC**

Department	Excellent	Good
Procurement		1
IT	1	
Finance	1	
HR		1
Kenya Demand		1
Kenya supply		1
CGI		1
EAML		1
UDV		1
Total	2	7
%	22%	78%

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Table 4.1 shows the number of transactions processed at the organization in the year 2000 before moving to a shared services strategy and the year 2009 (after moving to a shared services strategy).

**Number of Transaction processed before and after moving to a shared service centre.**

In the year 2000 (before SSC), the average number of manual journal vouchers raised in a month organization reduced by about 70%. The average number of invoices processed reduced by 44%. The average number of days taken to produce monthly accounts reduced by 57%. The average number of days taken to fully process and pay an invoice reduced by 33%. All this has come through as a result of process re-engineering and knowledge sharing see table 4.2 below.

**Table 4.2: Transaction processing for the period before and after moving to a shared services environment**

<b>Item</b>	<b>Year 2000 (before moving to shared services)</b>	<b>Year 2009 (After moving to shared services)</b>	<b>% Change</b>
Average number of manual journal vouchers raised in a month	200	60	70%
Average number of invoices processed?	1600	900	44%
Average number of days taken to produce monthly accounts	7	2	57%
Average number of days taken before an invoice is finally paid.	90	60	33%

**Impact of the Shared Services Centre on Employee Headcount and Overheads**

The second study objective was to determine the extent to which the shared service strategy resulted in reduction in employee headcount and overheads. Table 4.3 shows the number of employees working in each of the nine departments for the year 2000 before moving to a shared services strategy and the year 2009 after moving to a shared services strategy. In all the nine

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departments, year 2000 had more employees than year 2009. This is an indication that moving to a shared services strategy led to overall reduction of 21% in number of employees. Based on the fact that reports from EABL show that the organization has recorded growth in performance over the last four years, it can be concluded that reduction in the number of employees resulted to efficiency.

**Table 4.3: Number of employees per department before and after moving to a shared services environment**

<b>Department</b>	<b>Number of employees in 2000 (Before SSC)</b>	<b>Number of employees in 2009 (After SSC)</b>	<b>% Change</b>
Procurement	25	12	52%
IT	20	13	35%
Finance	55	35	36%
HR	20	5	75%
Kenya Demand	185	165	11%
Kenya supply	260	238	8%
CGI	175	148	15%
EAML	138	122	12%
UDV	135	60	56%
Total	1,013	798	21%

**Annual overheads on salaries and wages before and after moving to shared services**

As shown in Table 4.4, annual overheads for salaries and wages in all departments were lower in year 2009 than in 2000 by about 8% despite the general annual inflation and cost of living adjustments on the salaries. It therefore emerges that moving to a shared services environment availed a better control on the salaries and wages costs.

**Table 4.4: Annual overheads on salaries and wages per department**

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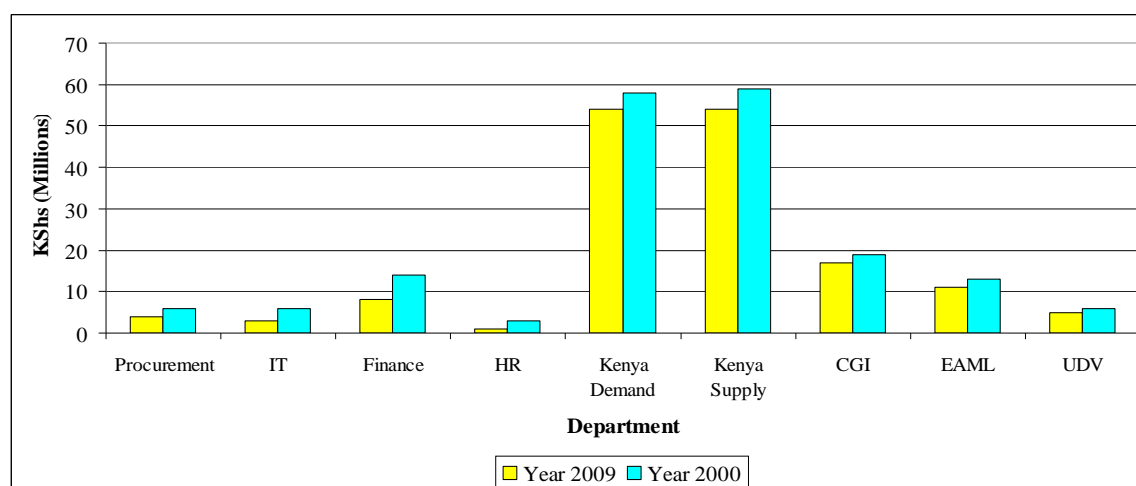
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Function	Salaries & Wages (Millions)		
	Year 2000	Year 2009	% change
Procurement	19	10	47%
IT	21	15	29%
Finance	58	40	31%
HR	9	3	66%
Kenya Demand	288	282	2%
Kenya Supply	394	393	0%
CGI	192	178	7%
EAML	144	140	2%
UDV	67	33	51%
<b>Total</b>	<b>1,191</b>	<b>1,094</b>	<b>8%</b>

**Costs incurred on overtime for the years 2000 and 2009.**

Figure 4.1 shows that for all the departments, the costs incurred on overtime were higher in year 2000 (before SSC) than in year 2009 (after SSC). In total, overhead cost for year 2000 was KShs 184 million, as compared to KShs 156 million in 2009, a decrease of 15%.

**Figure 4.1: Costs incurred on overtime**



**Costs incurred for conferences, training and travelling for the years 2000 and 2009.**

**Table 4.6: Costs incurred on conferences, training and travelling**

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Function	Costs incurred in KShs (Millions)					
	Conference		Courses& training		Travelling	
	2009	2000	2009	2000	2009	2000
Procurement	1	2	1	2	2	4
IT	1	3	1	3	2	3
Finance	1	2	1	2	3	4
HR	1	1	1	1	3	4
Kenya Demand	13	13	13	13	26	25
Kenya Supply	15	15	15	15	32	30
CGI	4	6	4	4	7	5
EAML	2	3	2	2	6	5
UDV	2	3	2	2	2	5
<b>Total</b>	<b>40</b>	<b>48</b>	<b>40</b>	<b>44</b>	<b>82</b>	<b>85</b>

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Change	-17%	9%	-3.5%

Table 4.6 shows that the costs incurred for conferences, training, and travelling were higher in 2000 than in 2009. This is an indication that moving to a shared services strategy led to a reduction on these costs. This can largely be attributed to the fact that as a result of concentration of this activities, there was no need for travelling and holding conferences. The employees also became experts in their fields as a result of shared knowledge rather than operating like competing entities.

**Costs incurred for telephone, medical and stationery for the years 2000 and 2009.**

**Table 4.7: Costs incurred on telephone, medical and stationery**

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<b>Costs incurred in KShs (Millions)</b>						
<b>Function</b>	<b>Telephone</b>		<b>Medical</b>		<b>Stationery</b>	
	<b>2009</b>	<b>2000</b>	<b>2009</b>	<b>2000</b>	<b>2009</b>	<b>2000</b>
Procurement	0.25	1	3	5	1	3
IT	0.25	1	3	4	1	2
Finance	0.25	1	8	11	4	6
HR	0.25	1	1	4	1	2
Kenya Demand	14	12	36	37	26	24
Kenya Supply	12	10	52	52	10	8
CGI	6	5	33	35	11	18
EAML	5	4	27	28	6	14
UDV	1	5	13	27	2	14
<b>Total</b>	<b>39</b>	<b>40</b>	<b>176</b>	<b>203</b>	<b>62</b>	<b>89</b>

Change	-2.5%	-13%	-30%

Table 4.7 shows that all of telephone, medical and stationery expenses declined after the organization moved to a shared services strategy by 2.5%, 13% and 30% respectively.

### **Impact of Shared Services Strategy on Inventory Management**

The third objective of the study was to find out how shared service strategy led to improvement in inventory management. All the nine (100%) departmental heads agreed that since moving to a shared services environment, inventory management had improved. Table 4.8 presents the indicators to show the extent to which inventory management had changed.

**Table 4.8: Inventory management indicators**

<b>Item</b>	<b>Year 2009</b>	<b>Year 2000</b>	<b>Variance</b>
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Stockholding Level (Billions)	2.6	2.4	+8%
Stocktaking costs (Millions)	3	4.5	-33%
Stock loss due to pilferage (Millions)	4	14.5	-69%
Stock loss due to stock obsolescence (Millions)	72	154	-53%
Insurance costs for stocks (Millions)	10	15	-33%

Table 4.8 shows that stockholding level was at KShs 2.4 billion in year 2000 and this rose to KShs 2.6 billion in year 2009, meaning that moving to a shared services strategy led to rise in stockholding level by 8% despite the impressive growth in turnover and production level. After moving to a shared services strategy, stocktaking costs reduced from KShs 4.5 million in 2000 to 3 million in 2009 reflecting a 33% improvement in stockholding costs. Stock loss due to pilferage reduced by a massive 69%, loss due to stock obsolescence reduced by 53%, while insurance costs reduced by 33% between year 2000 (before SSC) and 2009 (after SSC).

### **Impact of Shared Services Strategy on Procurement Costs**

The fourth research objective was to establish how shared service strategy at EABL has impacted on procurement costs. The nine heads of departments were asked to rate the impact of moving to a shared services strategy on procurement costs on a four point scale ranging from excellent to poor. Their responses are presented in Figure 4.2 below.

**Figure 4.2: Ratings of procurement costs after moving to SSC**



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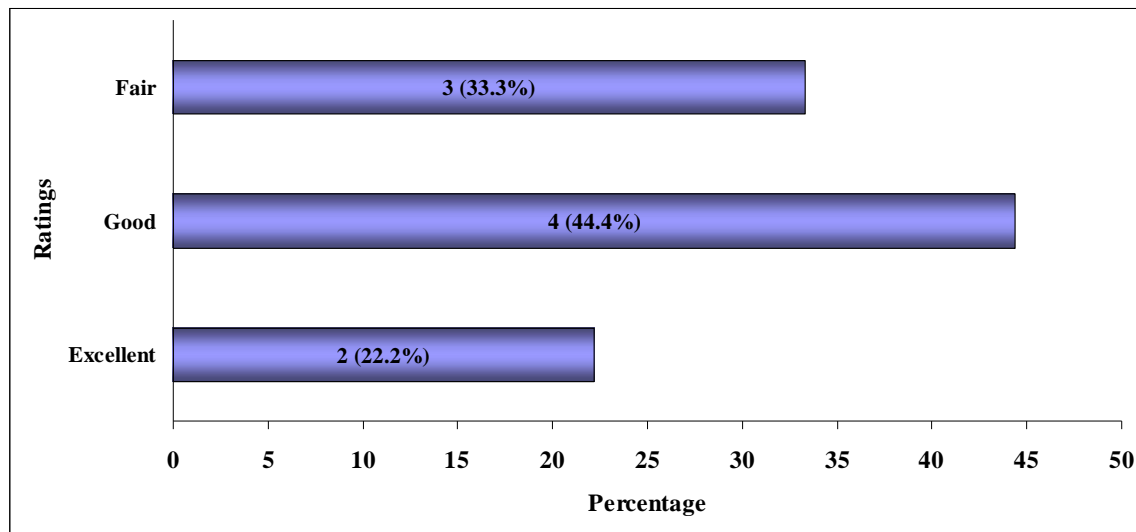


Figure 4.2 shows that 44.4% of the departmental heads rated procurement costs as good, 33.3% rated them fair, while 22.2% of the departmental heads rated procurement costs as excellent. Table 4.9 shows the impact of moving to a shared services environment on various procurement cost indicators.

**Table 4.9: Effects of shared services on procurement costs**

Item	Today –Year 2009	Year 2000	%Change
Average number of purchase orders raised (Annually)	18000	27000	-33%
Average number of days taken to conclude a contract	14	60	-76%
Average production cost per Hectolitre (KShs)	1000	925	+8%
Average cost of completing a purchase order in terms of stationary, printing etc (KShs)	0.85	2	-63%
Average period of having a purchase order fulfilled (days)	30	60	-50%

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Table 4.9 shows that before moving to a shared services strategy, about 27,000 purchase orders were raised annually, while after moving to a shared services strategy this reduced by 33% to 18,000 orders. The average number of days taken to conclude a contract reduced by an impressive 67% after SSC. The table also shows that the average production cost per hectolitre rose nominally by about 8% over the 8-year period. This is attributable largely to external factors such as the global economic meltdown, inflation, electricity and fuel costs etc all beyond the control of the company. Moving to a shared services environment also led to reduction in cost of completing a purchase order (stationery, printing etc), and period of having a purchase order fulfilled.

## **CONCLUSION AND RECOMMENDATIONS**

### **Conclusion**

Based on the findings presented above, it can be concluded that moving to a shared services environment has led to significant cost reduction at East African Breweries Limited. Specifically Shared services led to reduction in procurement costs, reduction in employee headcount and overheads, improvement in inventory management, and reduction of transactional costs. Besides, business processes have been harmonised and EABL is able to present a common face to all its customers

### **Recommendations from the study**

EABL as part of the wider Diageo group should look further to consolidating the processes within the wider Diageo group. Companies running their different functions as disparate competing entities should be encouraged to adopt shared services strategy to cut costs and operate more efficiently.

### **Suggestions for Further Research**

Since this study was conducted in only one organization, findings may not be generalized to other organizations. It is therefore important to study other organizations employing the shared services strategy to find out the impact the strategy has had in those organizations .A study on the challenges experienced by organizations in the process of moving to a shared services environment and the strategies employed to counter such challenges could also be useful.

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