



Contribution Margin: Why you Govern!

Put impact on contribution at the centre of your
Governance process

Margin no longer an issue: Sub optimal customer experience



What is Contribution Margin?

- It is the value your business expects the project or contract or customer relationship to deliver to the bottom line
- Accounting Definition
 - Contribution Margin or Controllable Income or Controllable Profit or Unadjusted Margin
 - Total Revenue – Total Variable Cost (on a contract or by customer relationship)
 - Total variable costs are the direct and indirect costs in delivering services
 - Overhead, costs of sales typically not included
 - The cornerstone of the business case
- Contribution Margin Ratio (%) = Contribution Margin/Revenue
- A target with business case and budget, implicit or explicit every business will have one
 - 20% for example, meet or exceed and everyone is happy

What is Governance

- Making decisions
- Decisions that define expectations, grant power, and verify performance
- Process and structures relating to consistent management, cohesive policies, guidance, and decision rights within a given responsibility area
- How the organization ensures it has the right evidence in front of it before deciding what to do
- Capturing, Analysing and Distributing all relevant Information about the Past, Present and Future of Services Relationships
- It is a capability that is learned and managed for. Some organizations are better at this than others.
- The very good ones are more profitable businesses.

Principles of Governance Excellence

- Accurate
- Consistent
- Timely
- Collaborative
- Structure
- Process
- Change Management
- Action Oriented
- Responsibility and Accountability driven
- Technology enabled

Why do Enterprises care about Governance

- Invest in governance capability for
 - High customer impact - satisfaction
 - High Financial leverage - contribution
 - Growth potential
- That Governance has direct and critical impact on customers is established
- A focus on contribution is becoming more central
- Satisfied customers and profitable business means growth for the Enterprise
- Leaders invest to secure high capability governance because of the direct impact on Customer Experience and Margins

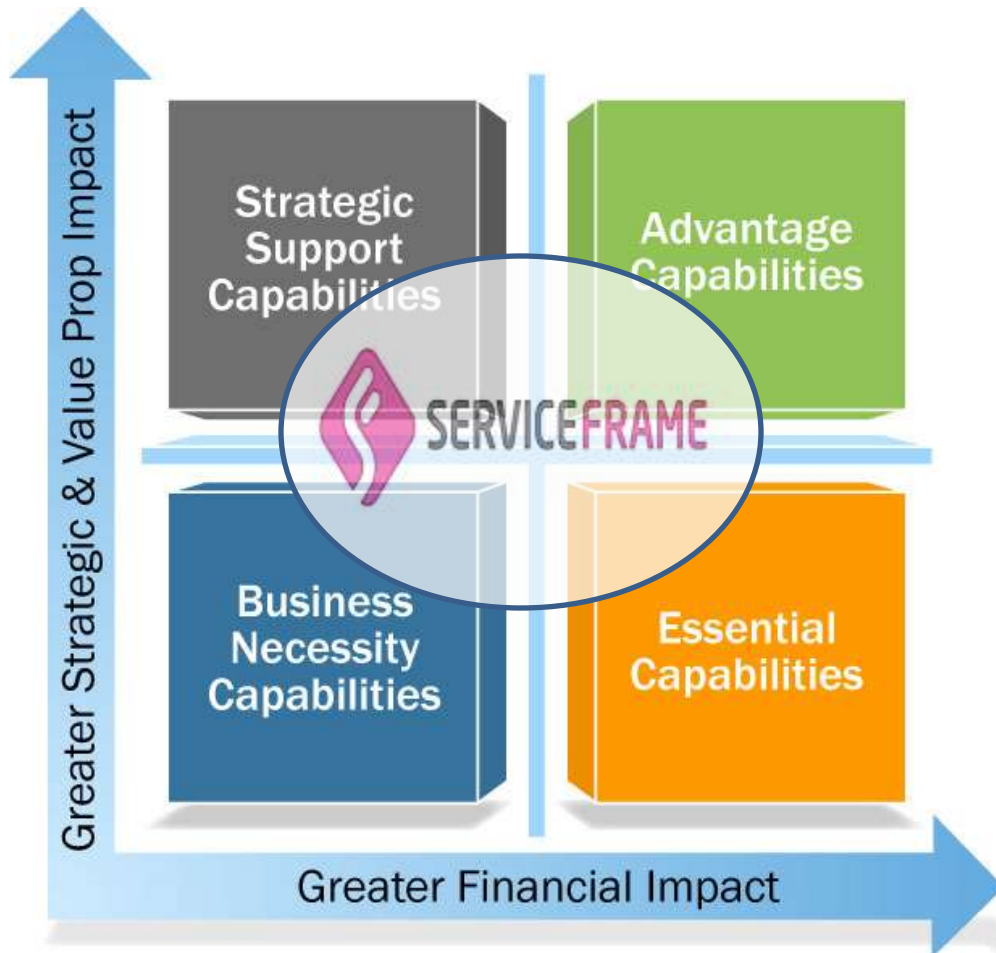
Finance Governance in Services

- Not in place of finance systems, standard accounting and cost management
- Customer Impact
 - Communicating value
 - Being transparent on cost
 - Highlighting opportunities for improvement in cost position and share benefit with customer
- Financial Leverage
 - Aligning service delivery with business objectives
 - Identifying and Communicating risks
 - Setting targets for margin enhancement
 - Compare and benchmark operational models from a value\delivery perspective
- Drivers of business growth

Invest in Capability

- What an organization needs to be able to do to execute its business strategy
- Enterprises build the capabilities that make strategy work
- Developing the experience and expertise of their people is what matters
- Strategic Capabilities: Capabilities in organizational planning, strategy, and investment
- Core Capabilities: The inventory of business capabilities that are identified as delivering the products and services that an organization offers to its market.
- Enabling Capabilities: The inventory of business capabilities that are required to support the business but not sold or offered to the market
- Governance capability drives service delivery and underwrites profitability
- Make capturing data on contribution margin core to governance capability

Capability



Deliver in the four quadrants:

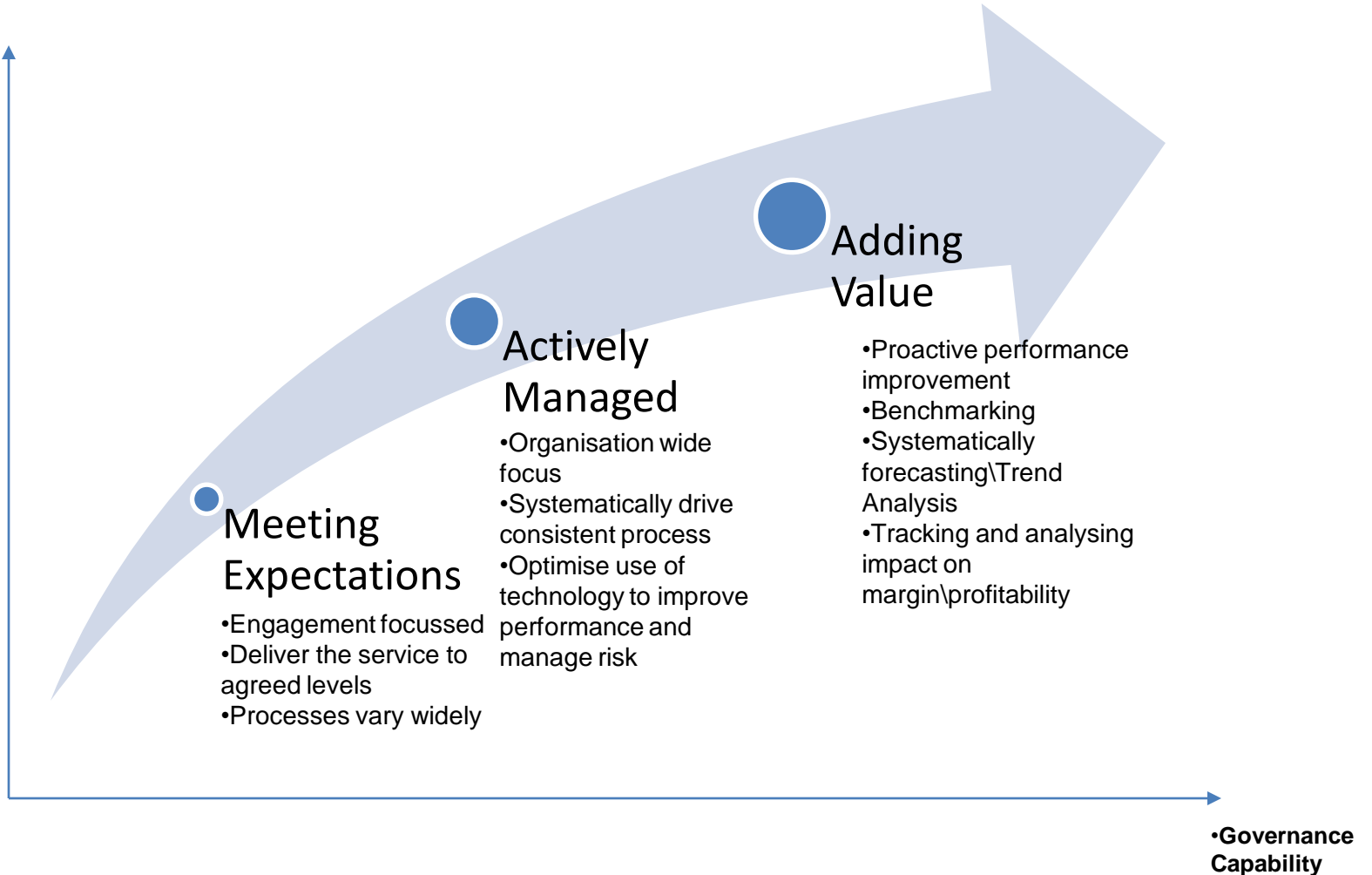
- Strategic – Customer Focus, Value, Growth
- Advantage – Differentiation, Competitive, Margin
- Business Necessity – Core competency for business
- Essential – Meet customer expectations

Philosophy

- Continuous service improvement, profitable deals and satisfied customers in Managed Services are driven by world class governance capability
- High performance organisations demand excellence in:
 - Performance Management – customer impact
 - Financial Management – business value
 - Relationship Management – customer impact
 - Threat Management – business value and customer impact
 - Knowledge management – business value and customer impact
 - Service Delivery – customer impact
- Metrics on finance impact are critical
- Unless you are capturing, analysing and distributing back to decision makers information on business value, cost, margin you are not delivering high capability governance
- Do this from the development of the first business case and never stop

Moving up the capability curve?

- Customer Impact
- Performance Improvement
- Financial Leverage
- Business Growth



What Impacts on Contribution Margin

- Direct Costs – people
 - Resource allocation - # and type of resources
 - Change
 - Predictability
 - Volatility
 - Redundancy
 - Latency
- Indirect Costs
 - Travel
 - Training
 - Other?
- Service Penalties\Rewards
- Customer Maturity
 - Competence\Capability\Experience of the people customers assign to the relationship
- Transition or Transformation
 - Costs elements change
 - Resource requirements may vary
 - Objectives, Expectations and Alignments differ

Optimizing\Minimizing\Maximizing as appropriate

Capture and Analysis

- Possible Calculators
 - Multipliers – a measure of the proportional effect of one variable on another
 - Loadings - interdependence between variables
 - Allocations – efficiency of resource allocation
 - Buffers – un-used capacity as contingency
- What moves the calculators up or down
- Statistical models, past experience, rule of thumb, a guess
- Capturing this information, analyse impact on contribution margin
- Predicting future direction, trend analysis, benchmark
- Decide on changes to protect\enhance margins and improve customer experience

Performance Improvement Plan

- Information alone will not drive improvement
- Incorporate into an Improvement Plan - a formal commitment to review and make change
 - Reviews, actions, assigned responsibility, explicit measures of success
- Engage stakeholders to change things that are negatively impacting cost.
- Who is involved? How do they receive the right information to help decision making?
- These are high capability activities
- If you are not explicit about communicating the value of what you do you are seen as low value and low capability
 - There is a choice to be made about how you represent your capability and value

Cost of Governance

- Governance is not free
- Typically between 5% and 9% of the value of a services contract*
- Information Capture – annual cost
- Information review and analysis – annual cost
- Reporting\information distribution – annual cost
- Technology Tools\Licenses – annual cost
- Opportunity Cost

- Use technology to manage this cost

Value to the Service Provider

- Money
 - Business Case, Changes over time
- Leadership
 - Thinking, Actions, Looking forward, Seeing Threats
- Strategy
 - Alignment, Direction, Support
- Information
 - Analysis, Benchmarks, Comparisons
- High Capability Governance delivers value

Summary

- Capture information on the elements that can impact contribution
 - Do this as early as possible – in the business case ideally
 - Measure constantly, analyse and understand trend, direction, scope
 - Communicate and support decisions to make change
 - Enable through technology
 - Establish a High Capability Governance reputation
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- ServiceFrame enables High Capability Governance delivered by Technology

Contact ServiceFrame

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- Product Overview – www.serviceframe.com
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