

# Studies regarding the Ways to Decrease the Expenses in the Area of Industrial Business

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*Abstract:* - Against the backdrop of the economic recession which makes many industrial businesses reduce their activity volume, the article deals with the problem of expense limitation. The subject is present in many theoretical works that care papers introduce the issue of costs and processes to reduce them. However, they do not specify the circumstances in which it is compulsory to reduce expenditure and those where this goal is optional. Also, there isn't a logical sequence of reducing expenditure and a minimum value of the costs, below which they cannot be reduced without affecting the activity of the company. Thus, the paper aims to determine the situations in which decreasing the costs is compulsory, as well as to identify a methodology to reduce them by analyzing the main operational expense categories.

*Key-Words:* - backdrop of economic recession, expense limitation, decreasing the costs

## 1 Introduction

Achieving the objects of each operator requires the use of all the elements that make up the labor process. Some of these are consumed in the production process or marketing, another part is depreciating, while others must be paid. Regardless of how they can be used, the material, financial resources, human or environment resources used in the enterprise generates costs. The expenses are the money expression of the consumption determined by obtaining and selling the material goods, execution of works and service.

The recovery of the expenses made in order to acquire goods, is made by their inclusion in the cost of the obtained production, the selling and cashing its value from the clients.

As a general objective, permanent or temporary, cost savings are a concern that is found in the majority of families, businesses, state level and state institutions. Of businesses listed, the article is circumscribed to private entities, regardless of their capital, business size or scope of activity undertaken. The costs are reflected in all businesses, since it is a goal that will generate a competitive advantage [2] [7].

For research, there should be started from meeting its objectives. In relation to the theme of the work, the research is aimed at achieving the following

objectives:

- setting the position of the reduction in expenditure compared to the fundamental objective of the enterprise;
- determining the situations where the enterprise must reduce costs;
- identifying the categories of expenses that can be reduced;
- example of the scientific approach in a real data structure.

Achieving the above is done based on theoretical and practical elements present in the literature.

## 1.2 The relationship between the expenditure and the primary objective of industrial business

The fundamental objective of the company must be identified in the economic theories or in the financial statements. Summarizing the conclusions therein, there may be remembered that the fundamental objective of financial management is to maximize the enterprise value. Its measuring led to two formulations:

- patrimonial, according to which maximizing the patrimony accumulated in the previous exercises is aimed at. It is connected to the net situation (net assets) determined as the difference between total assets and the total debts contracted by the company.

$$NS = Total\ assets - Total\ debts, \quad (1)$$

where NS is the net enterprise situation.  
 - financial, meaning maximizing the actual value of the future assets expected to be obtained, during the company life time, with the help of the present patrimony. Thus, the financial value is determined based on the gain expectancy, the company shall bring, with the patrimony accumulated up to the present [9]:

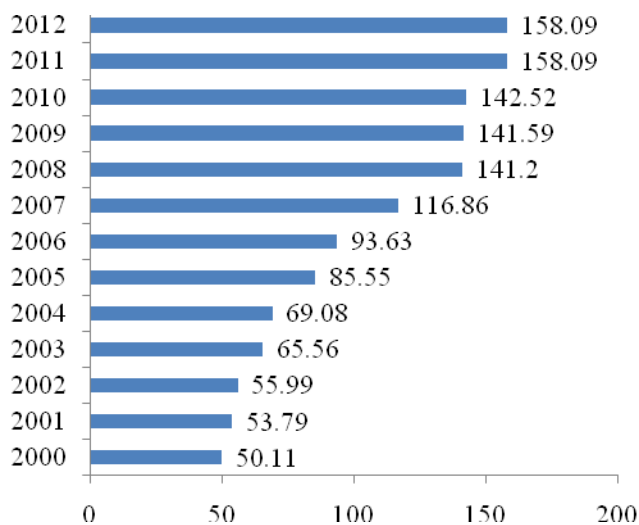


Fig. 1 Minimum wage between 2000-2012 years

$$FV = \sum_{t=1}^n \frac{CF_t}{(1+r)^t} + \frac{RV_n}{(1+r)^n}, \quad (2)$$

where:

FV is the company financial value; CF future cash-flows generated by the company during its life span;  $RV_n$  estimated residual value, remaining after n years of economic life; r discount rate;  $t = 1... n$  company economic life span.

From the background there is drawn a conclusion that reducing costs is not the primary objective of the company. If spending cuts should be the primary objective of the company, then one should always follow their reduction over time. For example there are considered interest expense arising from loans made by the company in the current or previous periods. These expenses may be void if the organization waives loans. Absence of leverage, will leave the company only alternative equity financing activity in solution that ensures stable growth, but slow.

To this conclusion there should be added that, in

analyzing various types of consumption, bear in mind that, usually for efficient operation, making an income requires expenditure and vice versa. Expenditure-income relationship is valid default for operating activities, crucial for industrial enterprises, as this activity has approximately 95% of total [3]. Exceptions to this rule occur if financial expenses and exceptional not generate revenue as revenue realization not necessarily involve items of expenditure.

From the above it results that any analysis of expenditures, total or by category of activities shall be carried out separately, but in close correlation with the income categories whose accomplishment contributes.

### 1.3 Identifying solutions to reduce operating costs

To increase the competitiveness, many works recommend cutting costs. The challenge can hardly be translated into practice in an emerging economy where inflation shown in Table 1 remains stubbornly high and the minimum wage (or average) the economy is growing [8]. The presence of inflation causes price increases of raw materials, materials and energy resources is often, fundamental to any industrial product.

Table 1. Inflation rate between 2000-2012 years.

Year	Inflation rate (%)	Year	Inflation rate (%)
2000	45.7	2007	4.84
2001	34.5	2008	7.85
2002	22.5	2009	5.59
2003	15.3	2010	6.09
2004	11.9	2011	5.79
2005	9	2012	3.33
2006	6.56	Previous year =100	

Figure 1 shows the value of the minimum wage established under the laws of Romania. There is found an increase of the minimum wage, which represents the wage policies of public and private employers [4] [5] [6]. The data presented shows that market due to objective causes, increase the manufacturing costs of industrial products, while the literature shows the need to reduce their. Enterprises in the economic environment can be delineated into two categories, depending on the economic and financial results obtained:

- A) Profitable enterprises that can be delimited in:
  - A.1) Enterprises characterized by high rates of earnings, that record permanent cash surpluses over

several years in a row. In their case it is not compulsory to save money, but rather their supervision.

Their main concern is to develop own activity, primarily, through investment.

A.2) Low return businesses or those that are easy to cover the accumulated loss of previous years. The fact that those businesses fall into such a category is because the market has brought here, due to lower revenues.

Actions aimed at increasing incomes are desirable, but they usually theoretical. For them the best is to analyze costs and identify ways to reduce some of these;

B) Unprofitable businesses characterized by the profit absence. They can be divided in:

B.1) Small loss-making enterprises that can be covered in future years profits. By increasing revenue, actions will be geared towards identifying solutions to reduce expenses.

B.2) Enterprises that confront with significant losses which have taken equity accumulated in previous periods.

The analysis may result in expenditure solutions, but should be done in a prior period.

Rather, these companies are turning to reorganization or recapitalization by shareholders or shareholders' agreement.

Figure 2 shows that reducing costs is required for businesses that are characterized by low profitability or lack thereof, reflected by loss but not covered equity value.

There were previously detached a few rules for the identification of undertakings and where it is necessary to reduce costs. Before reducing the costs, the first direction in taking action will be in the area of incomes, aiming to increase them. For this purpose should be considered, such as:

- identifying new markets and customers;
- development of price strategies;
- promotion of products;
- proper substantiation of prices;
- granting of benefits to loyal customers etc.

Of course, these actions will be accompanied by reduction of costs according to what logic will be removed.

Reducing costs will start from total expenditure. In this respect the procedures made available by literature are [3] [7]:

- a) dynamic analysis of costs;
- b) study of the structure and composition of expenditure;
- c) calculation of efficiency of expenditure rates;
- d) the application of factor analysis models.

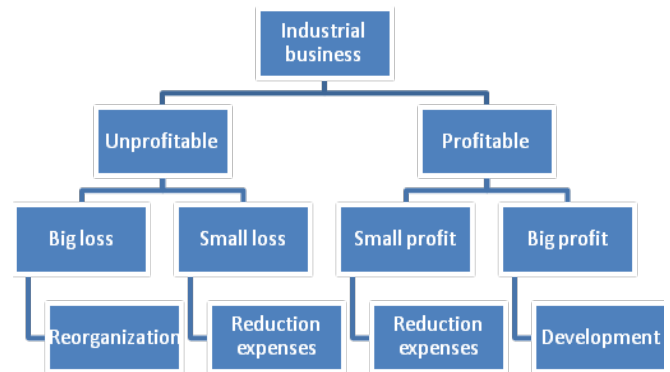


Fig. 2 Position of industrial business depending on the economic and financial results

Among the most effective are the processes listed under point c and d. To this end, calculate and model the dynamic efficiency rates of total expenditures by reporting their volume, total revenues for the respective periods. Since the process will always lead to the need to increase revenue, such solutions are not listed as they were previously treated. Both income and expenditure are held in financial accounting, according to their nature, the three activities: operating, financial and exceptional. The first examined are the total expenditure to be reported the total revenues constituting an efficiency rate. Tracing the evolution of the expenditure total revenue is at an average rate of efficiency of the overall expenditure (or cost per 1000 lei total revenue) determined by the relationship:

$$R_{TE} = \frac{\sum_{i=1}^n E_i}{\sum_{i=1}^n R_i} \cdot 1000 \text{ or } R_{TE} = \frac{\sum_{i=1}^n g_i \cdot r_{ei}}{100}, \quad (3)$$

where  $R_{TE}$  represents the average rate of efficiency of the overall expenditure;

$\sum_{i=1}^n E_i$  the amount of expenditure by category of activities (financial and exceptional service);

$\sum_{i=1}^n R_i$  the amount of revenue by category of activities.

$g_i$  incomes structure;

$r_{ei}$  individual rate of efficiency.

Reduction of the rate level equals with an increased efficiency with which there were used financial,

human, material and environmental aspects of the company. Similarly increasing the value of the report shows a decline in the efficiency of the enterprise [7]. Such a procedure does not usually lead to solutions, but rather an overview of the company's revenue and expenditure and on the formation of the gross income. Therefore analysis should continue, observing previously identified. For example it is considered state of the Table 2. Applying relations 2 lead to results in Table 3. The efficiency ratio of the total expenses increased with 73.832 lei compared to the preceding period, aspect interpreted as negative as it leads to a decrease of the company profitability. It is both a consequence of the decrease of the total income, from 955983 to 943287 lei and of the increase of the total expenses in the same period from 780091 lei to 839376 lei. From the two factors considered, we determine that for a 99% percentage the evolution of the analyzed indicator is the result of the efficiency rates related to the three activities: operation, financial and exceptional. Most of the efficiency rate of the total expenses is the cumulated result of the growth of all efficiency rates. Among them, operation detaches an activity whose weight increased from 88.41% to 87.61% while the afferent efficiency rate increased from 846.189 lei to 887.455 lei.

There will be proceeded to analyze operating expenses, whereas they held at the industrial business, the largest share in total expenses. It will calculate the average efficiency of operating expenses determined by the relationship:

$$R_{OE} = \frac{\sum_{i=1}^n OE_i}{\sum_{i=1}^n OR_i} \cdot 1000, \quad (4)$$

where  $R_{OE}$  represents the average rate of efficiency of operating expenses;

$\sum_{i=1}^n OE_i$  the amount of operating expenditure by types of activities;

$\sum_{i=1}^n OR_i$  the amount of revenue from exploitation by types of activities.

Categories of expenditure shall be determined with the largest share in the total. Any solution to reduce them will result in an economy that will result in relative profitability. From the structural point of view the running costs comprise the following items:

- a) expenses relating to the consumption of raw materials, auxiliary materials, fuels etc.
- b) the costs of the work and services performed by third parties;
- c) expenses with taxes, fees and similar payments incurred by the patrimonial unit;
- d) staff expenditure;
- e) expense with depreciation of fixed assets;
- e) other operating expenses etc.

From the previous enumeration one can see the large number of operating expenses. Theoretically we can create efficiency rates or other computational models and analysis.

## 4 Conclusion

Reducing costs is not an objective in itself, but rather as one particular provision under certain circumstances they may be at the enterprise. In situations where we have to reduce expenses the article makes available some logic to this approach that applies to finding concrete solutions.

In most cases, in order to reduce the costs, there is proceeded to their analysis. Always spending it will report revenue and not vice versa, causing the emergence of revenue expenditure. The starting point is the total expenditure and the approach continues with the categories of expenditure that hold the largest share, up to finding solutions.

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