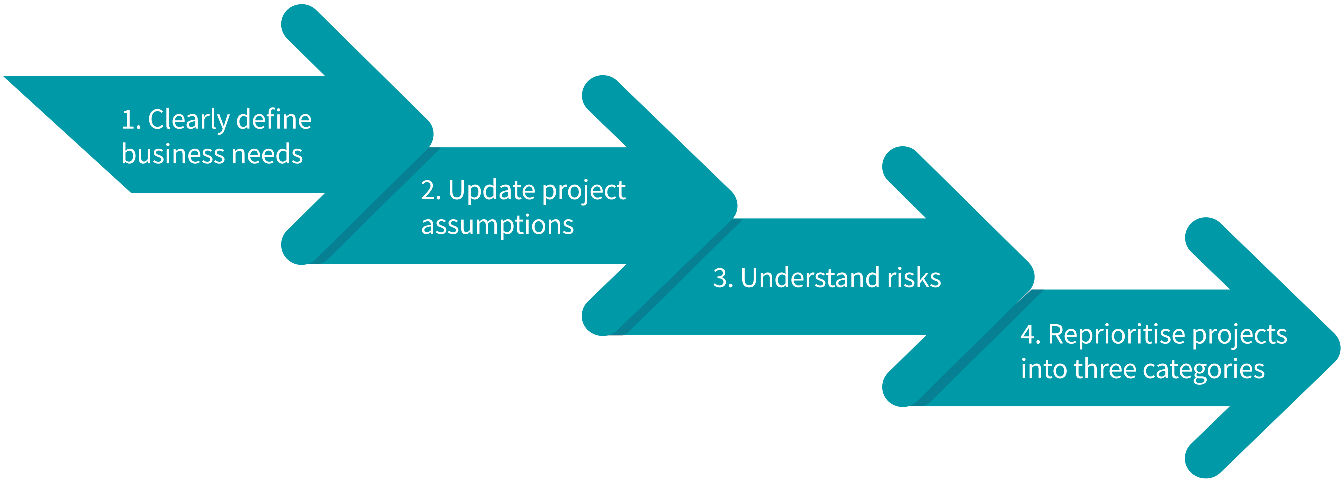
Sustaining capital - vol 1 – realigning your capital portfolio

- With the current pandemic, organisations are urgently looking to improve liquidity and reduce costs
- Realigning your capital portfolio to select essential and high-return projects can quickly reduce capital requirements, whilst also increasing capital efficiency
- Organisations can quickly and successfully navigate capital portfolio realignment, maximising value and business impact by clearly defining business needs, updating project assumptions, understanding risks and reprioritising projects into three key categories

In response to the current challenges, many organisations are now looking to reduce costs and capital expenditure to free up cash and improve profitability. Sustaining capital is an obvious target as it represents a significant portion of expenditure, but also tends to be less rigorously critiqued compared with operating costs.

When money is tight, the easy answer is often to stop these projects; however, this affects future operations and often reduces productivity when demand and production ramp back up. Optimising your capital portfolio will ensure capital is allocated to critical projects, enabling the delivery of greater value from a lower spend base.

Four key considerations when realigning the capital portfolio



1. Clearly define business needs

What was 'essential' a month ago may not be now. Organisations need to understand how the current economy affects available capital, dictating how much planned spend needs to decrease. This should also inform the priorities within the business – for some, growth projects may become less relevant if commodity prices are falling, while others may need to rapidly increase capacity, so expansionary capital spend will become important.

2. Update project assumptions

Once your business needs are understood, each project in the portfolio can then be reassessed to ensure it meets core business needs with available spend. This should include an assessment of the current project status, stage and committed spend, as well as any potential cancellation costs.

3. Understand risks

Ensure robust risk scenarios are built into assessments to protect against contingencies that could impact project delivery (e.g. extended lockdown, non-essential employee return to work, resurgence of COVID-19).

Evaluating supply chain and resourcing stability is critical to the success of any capital project. Identifying emerging risks posed by the pandemic will allow companies to determine feasibility of project completion and develop mitigation and management plans. Be specific and consider all risks, such as:

- Have suppliers rediverted resources/manufacturing to COVID-19 essential products?
- Are materials airfreighted and, if so, are those airplanes still running?
- How is employee safety managed onsite?
- What new practices or shift structures need to be instilled to mitigate the risk of virus spread on the worksite?

Know that things can, and will often, change overnight during this time – establishing clear tracking and reporting of risks and risk management plans are equally important to identifying risks. Conduct regular reviews to identify and resolve issues that may arise – before they become major problems.

4. Re-prioritise projects into three categories

Projects should be selected on the absolute ‘must haves’ which are required to maintain a license to operate (safety, environment, compliance) and deliver the highest return (best ROI vs. risk). This prioritisation should look across all sites, rather than just within sites.

For each individual project, there are three potential outcomes:

- **Expedite,** but do so safely, complete work remotely/offsite where possible and ensure the full safety of essential workers at all times
- **Put on hold** with a clear outline of risks and future deadlines (e.g. when does a decision need to be made to restart, when should project be reassessed)
- **Cancel,** where the assumptions and requirements of the project are no longer valid based on the current environment (e.g. project to increase oil production)

Conclusion

While most organisations are making cuts to capital spend, those that act quickly to realign the portfolio will also see an increase in capital efficiency – maximising value and impact for the business. To ensure the right project decisions are made and aligned within the business, organisations should take immediate steps to clearly define business needs, update project assumptions, understand and plan for risks and reprioritise projects by outcomes.

Learn more: Cutting Capex in a crisis

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