

Activity Based Management – the Rubik’s Cube of Business



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Synopsis

Your company has a general ledger and financial reporting system which can analyse the profitability of the various “drivers” of your business... or can it?

Ask your system...

- Who are your **most** profitable managers? Your **least** profitable managers?
- Who are your ten **least** profitable customers? How do these results compare with budget?
- Can you rank your ten most profitable clients in order of profitability?
- Which projects are running over budget?
- Have you spent or committed more than the funds allocated for a certain programme / project?

How easy is it to extract this information? How long does it take? Can management collect this information from a self-service Intranet kiosk?

An effective, timely and affordable ABM system is critical to the efficient management of most businesses. This article highlights issues such as system design and software selection to help you build an ABM system and tailored it to the needs of your business. But the key is... to keep it simple.



The Problem... “Analyse This”

In the movie “Analyse This” Billy Crystal discovered that, in the real world, problems don’t present themselves in neat and tidy bundles which can be analysed by the simple tools he was taught to use at college. Real life is much messier, more dynamic and a lot less predictable than the world of theory. This realisation certainly holds true when you try to analyse the performance of a business.

Your company has a general ledger and financial reporting system which can analyse the profitability of the various “drivers” of your business... or can it?

A typical hierarchical chart of accounts structure looks something like this:

Subsidiaries.....
 Divisions.....
 Departments.....
 Regions.....
 and it may extend to cover.... Product and/or Service Groups..... etc.

But what if you want to analyse profit by product range across the whole group, regardless of location or department? Is one region performing better than another? Do certain products perform better in some markets? How do your marketing campaigns affect profitability?

Conventional accounting reports are analysed into a hierarchical format, typically reflecting the organisation’s chart of accounts which someone designed ages ago. In theory, these reports allow you to “drill down” and analyse what’s going right and what’s going wrong in your business. However... in the real world, problems and opportunities can occur anywhere in a business... and it is purely a matter of luck if problems can be detected through a hierarchical analysis of the business.

Can your existing management reports answer these questions...

- Who are your **most** profitable managers? Your **least** profitable managers?
- Who are your ten **least** profitable customers? How do these results compare with budget?
- Can you rank your ten most profitable clients in order of profitability?
- Which projects are running over budget?
- Have you spent or committed more funds than were allocated for a certain programme / project?
- Which suppliers are your most profitable sources?
- How easy is it to extract this information? How long does it take?

One simple and effective method of managing to improve your organisation is to analyse the best and worst elements of your business... promote the best elements and improve or curtail the worst. But how do you detect this information? What are the interdependencies? Perhaps your business has a “loss leader” strategy, but can we measure the loss and justify it relative to the rewards?

Realistically, the drivers in your business might be something like... subsidiaries, divisions, departments, geographic regions, product ranges, products, services, plus... Customers, Manager’s performance, suppliers, projects, fund source, tenders, advertising/marketing campaigns, promotions, production lines, manufacturing processes, etc. Unfortunately there is no neat hierarchy which logically links these elements together in a logical fashion.

You often hear about managers wanting to “slice and dice” their information. But how?

If your organisation is a government or non-profit organisation then you may have a whole extra raft of reporting problems ... reporting against grant allocations, as well as different reporting periods and deadlines required by other organisations who require reports. It’s as though your management reporting system must serve many masters. You must analyse your business to meet the needs of these “masters” or else you may not be able to justify your need for funds next time around.

The question is... how to derive this information... **efficiently?**

The diagram is divided into two panels. The left panel shows a 3D Rubik's cube with faces labeled 'Products', 'Projects', 'Managers', 'Customers', 'Regions', and 'Departments'. Below the cube are labels for 'Subsidiary', 'Services', and 'Division'. The right panel shows a person's head looking into a colorful Kaleidoscope. The Kaleidoscope's segments are labeled with business terms: 'Customer', 'Managers', 'Suppliers', 'Division', 'Customers', 'Suppliers', 'Regions', 'Services', 'Process', 'Tenders', 'Prod. Group', 'Process', and 'Costs/Grants'.

Think of your business as a Rubik’s cube, and each face of the cube gives you a different view... This would give you six “faces” for your business. Depending on which view of your business you want, you can twist the cube to see the view you want.

What if your business has more than six faces? Perhaps you need a viewer that is something like a Kaleidoscope?

If you are used to the “drop down box” or “filter” concept of software, you might imagine all your business drivers lined up in a row, and you can then select the elements for further analysis...

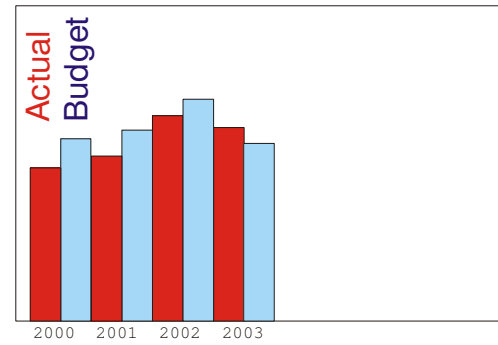
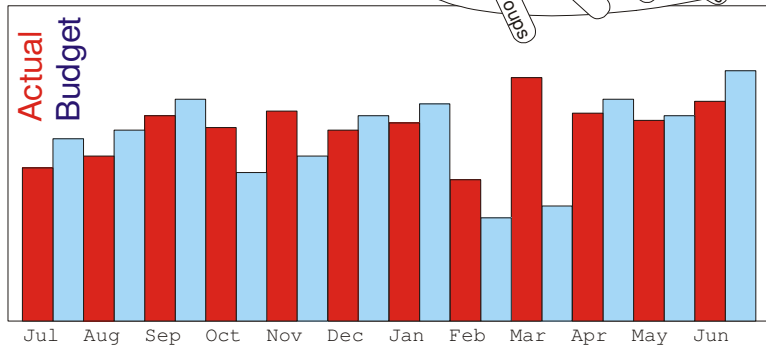
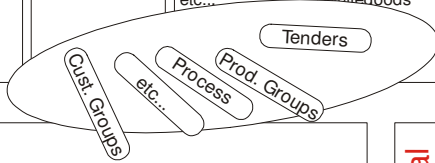
From Sales System

From General Ledger

From Purchasing System

Other statistics & KPIs

Regions ▼ Australia NSW NT SA Tas Vic Qld New Zealand Saudi Arabia etc...	Customers ▼ ABC Industries Beta Corp Delta Services Epsilon Ltd Gamma Corp etc...	Managers ▼ Bill David Mary Robert Zelda etc...	Subsidiary ▼ Company One Company Two Company Three etc...	Division ▼ Boutique Bulk Supermarket Wholesale etc...	Department ▼ Books Clothing Electronics Furniture Whitegoods	Fund Source ▼ Govt Grant 1234 Govt Grant 3333 Joint venture ABC Joint Venture XYZ etc...	Suppliers ▼ Acme Charlie Corp Jones Ltd Smith Corp etc...	etc... ▼
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In reality, most software packages do not allow you to perform this analysis. In fact, they don't even capture the information in the first place.

How to build an Activity Based Management system

The first step in building an ABM system is to capture the information. If your business is very simple then you may be able to achieve this using a low cost accounting system and a hierarchical chart of accounts. For most medium sized and larger organisations this won't work. At a minimum, they need to add modules for purchasing and sales. If the organisation is not a simple buy-sell business, then they will need something smarter... where each business transaction can be analysed into its critical elements.

My own work is as a specialist in Accounting system selection and integration. The sad fact is that most of the packages available on today's market do **not** allow a straightforward and logical breakdown of this information. In some cases they may capture the information, however they do it in such a way that it makes reporting and analysis unnecessarily complex and difficult.

It is beyond the scope of this article to go into detail about the method by which some software packages capture the necessary information... this depends on the complexity of your business, the software which is available and your budget. Our own company and others like it can provide guidance on which business packages can provide an ABM facility. One major fallacy is to think that more expensive accounting packages will do a better job than cheaper ones... It ain't necessarily so!

Most accounting packages do not capture the information you need unless some extra "tweaking" has been performed. Experts in accounting and business systems can add fields or tailor fields to capture the activities which are applicable to your business. But watch out! When they make these changes, be sure that it does not risk your future compatibility with the mainstream product with regard to upgrades and support.

If you can't capture the fundamental elements of each transaction then you need go no further... it simply won't be reported adequately to enable strategic analysis.

So, for the sake of this review, let us assume that you have an accounting package which captures the relevant information. Now, how do we perform the analysis? This is the good news.

Today, most business packages have already achieved, or are moving towards compatibility with major database standards such as MS SQL or ODBC. If your package does not conform to one of the major standards then it's time to go shopping for a new package.

Let's assume that your accounting system has a compatible database.

Then, the question is... if you need to analyse your business by these different drivers... how do you achieve this without working around the clock fiddling around with spreadsheets? Surely in these modern times software can achieve this?

Fortunately the answer is yes. And the cost has fallen dramatically in recent times. There are a range of leading report writers available at a reasonable cost. The most popular one is Crystal Reports, Crystal Enterprise and Crystal Analysis. The Crystal range has a massive market share, however do not overlook some of the more specialised report writers which are sometimes programmed to simplify the process of report design.... they may anticipate the required data elements without having to navigate the innards of your database. The hard part of designing your ABM reports is finding the information you need inside your database. With fields spread out through the database it is highly likely that you will need the help of a specialist to guide you to where the data elements can be found inside your database.

Once again, do not assume that the best products are the most expensive.

Keeping it simple

A few tips to keep it simple:

- Don't try to create too many levels of analysis. You need to strike a balance between setting the number of elements to analyse your information and what is practical. As a rule of thumb, in the general ledger you should avoid having more than five levels of analysis.
- Do not create a "humungous" chart of accounts. If your accounting system is based on a hierarchical chart of accounts (and most accounting systems do work this way), then it's time to go shopping for a new accounting system. If you are serious about Activity Based Management then you will be best served by a system which allows you to set up the different elements of the coding structure as independent units. This type of general ledger can reduce the number of accounts in your GL by over 90%. This is an enormous labour saving. No chart of accounts should have more than a few hundred accounts in it... otherwise it is too laborious and too confusing. Aim to keep it tight and have around 100 accounts in your general ledger. This might sound impossible, but if you have a suitable accounting matrix coding structure which lends itself to Activity Based Management, it can be achieved, even for large organisations. The secret lies in using the activity codes for further analysis.
- Your analysis should not be confined to financial data. Build into the model other Key Performance Indicators which are relevant to your business: Measure product quality. Find out what is the level of customer satisfaction? How many new customers this month?
- If your business system database does not provide adequate access to your data, all is not lost. You can create a "data warehouse". Once, this meant spending a lot of money. These days, a simple MS Access or MS SQL or other compatible database can provide an excellent data warehouse, in combination with a quality report writer suite.
- Learn about the leading report writers... try to cut down on your use of spreadsheets and learn about products like Crystal and similar low cost report writers. You need the right tool for the job... spreadsheets are a clunky and inefficient way to provide ABM reporting.
- Use the leverage available from Web technology. The best reporting and analysis tools provide a web interface, so you can deliver information to your Managers through your Intranet Kiosk. This saves you time deploying the information to desktops, maintaining report versions, and it also saves on costs. For example, with Crystal Enterprise, the basic reporting tool includes a free five concurrent user licence for web clients.
- Stop!!! If you find yourself using the "cloning" facility in your chart of accounts, to create more and more accounts under your hierarchical structure... please check if there is an easier way. If that really is the only way to dissect your financial information, perhaps you need to put pressure on your software provider for a smarter system, or to upgrade to a smarter system which can efficiently cater for ABM.

Conclusion

The results from creating an Activity Based Management system are outstanding:

- Managers can access their information through a self-service "kiosk". This saves time having to create "ad hoc" reports for management. This saves time for the information providers.
- The organisation can find the "hot spots" in business activities... capitalise on the successes, and put out the spot-fires where there are problems.

Many businesses today are becoming more service oriented and more complex. As a consequence their need for an ABM strategy in business continues to grow.

An effective, timely and affordable ABM system is critical to the efficient management of most businesses. And remember, the system will need to be designed and tailored to the individual fingerprint of your business. There is no "one size fits all" solution. And keep it simple!

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