BUSINESS PERFORMANCE
ADVANTAGE

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Our mission is to provide information and strategies to business owners and managers for improvement in the effectiveness of its business management so that key objectives can be realized.

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Make the Move to Dynamic Forecasting

Is your budget obsolete in two months? The traditional corporate budget process focuses on what managers are allowed to spend to accomplish their goals and not what resources they require. Budget plans can be costly to prepare, starve departments that have valid needs, incorporate last year's inefficiencies and fail to identify waste and respond to a business' strategic objectives. However, companies can develop more realistic, dynamic budgets based on predictive planning. One way to do this is to use activity-based costing (ABC)—basing company plans on fluctuating needs related to demand rather than on historical data.

Here are some budgeting tips to keep in mind that incorporate ABC principles.

- Don't limit yourself to the current situation defined by predetermined spending limits. Begin the budget equation with the outcomes you expect—profit, for example—measured against customer and management demands that vary in mix and volume over time. Don't let your budget stay frozen; revisit it as needed in response to marketplace conditions.

- Budget management and cost management are not synonymous, so don't confuse them. Formulate budget strategies according to two questions: What should we be doing, and how should we do it?

- Then inject costs into the equation. Using activity-based-cost estimating helps you relate what-if scenarios over time to the overall impact of expenses on the organization. For example, are you going to open a new warehouse? To estimate the level of spending required in the future, you should match future capacity (what's currently available vs. what's required) with estimated needs (forecasted customer demand).

- Activity-based-cost management is not a replacement for general ledger accounting. But if your general ledger software does not convert spending into useful managerial information, use an ABC model—based on resources, work activities, process costs and final cost objects—to reflect market, product, service-line, channel and customer-oriented decisions.

- No one knows in advance how simple or complex a company's first ABC model needs to be. Many make the mistake with their initial ABC system of plugging in too many details before learning how to apply the data or what the accuracy requirements are. Instead, improve the usefulness of the results by understanding that such predictive planning depends on constructing a cost-assignment network that traces how outcomes—such as products or orders—consume resource expenses with a cause-and-effect relationship.

- Organizations always want to understand where they make and lose money. To get a better picture of this, design budgets that do not inhibit managers' flexibility to meet objectives. Develop plans that are feasible, determine what specific resources are needed to execute them, then compare the plans' projected results with current performance to manage profit margins.

- Successfully implementing ABC depends to a large degree on managing organizational behavior. Avoid resistance from employees and managers that can jeopardize the acceptance of the new methodology or technology by following these rules:

  – Use a rapid prototyping pilot program to quickly implement a summarized ABC model. Don't necessarily start with your most technologically sophisticated employees; this will stigmatize the project by making it look like it's for tech gurus only.

  – Get the support of an executive sponsor and find a champion to create interest in ownership of the information and its uses.

Make the Move to Dynamic Forecasting (cont.)

- Make sure there are end-users who really need the data—design the system with the ends in mind.

- Don't be afraid to combine art, craft and science in constructing your ABC model. One that is successfully prototyped can quickly be redone with more detail and accuracy so users readily begin to see how the ABC data relate to the problems they are trying to solve. ABC models can provide valuable insights within weeks that aren't visible from traditional data

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