

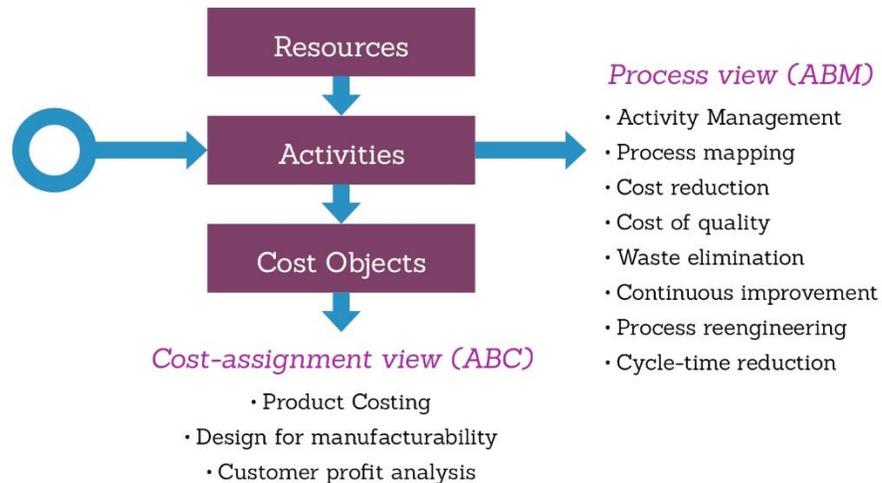
Do you know what it actually costs to run your business and what drives these costs?

It is no secret that every decision maker is expected to deliver more output with less resources in today's economy. Yes, using technology and improving the efficiency of the operations are some of the focus areas that can be used, but how can finance contribute to this never-ending drive to deliver more with less resources?

Knowing what the true cost drivers are and measuring the actual cost in detail is a very powerful management tool that can be used to improve the bottom line. Using these actual costs from the identified cost drivers and modeling different scenarios empowers decision makers to make informed decisions.

For those unfamiliar with the management practice, **Activity-Based Costing & Management (ABC/M)** is a discipline that focuses on the efficient and effective management of activities as the route to improving the value, be it a product or service. Activity based management draws on activity based costing (ABC) as its primary source of information. Using activity based costing, resources are assigned to activities and then activities are assigned to cost objects based on the use or consumption of activities.

ABC/ABM is built on two axes. The *vertical* view is the snap-shot view, and the *horizontal* view reveals the causes and results of costs.



As Peter Drucker put it, “Efficiency is doing things right; effectiveness is doing the right things.” Put differently, effectiveness determines if the ladder is against the right wall, while efficiency is how fast you climb up and down the ladder. If the ladder is against the wrong wall, then it does not matter how fast you climb the ladder up and down!

The finance function can contribute great value to the organisation by leveraging ABC/M to provide more accurate analytic information to answer key business questions:

- Which of my products/customers are unprofitable?
- What are the main cost drivers?
- What are my supply chain costs?
- What are my support costs?
- What are my cost pool build up per product/process/channel/customer?
- What is my transport cost per SKU?
- What are the costly processes?
- How can I identify non-value adding activities?
- How can I optimise activities?
- How is funding utilised?

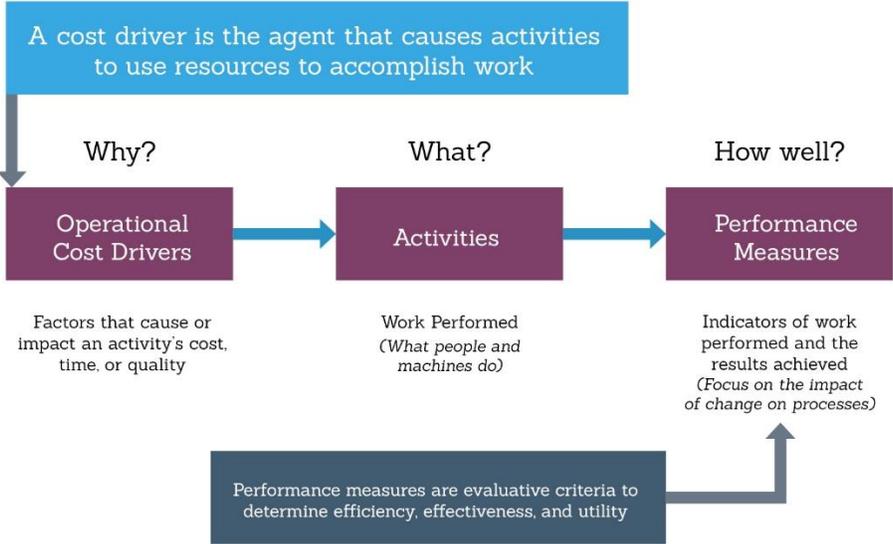
By using ABC/M, an organisation can gain a greater insight of how costs behave in their organisation and which activities create a significant amount of costs. Once you understand that you can then take action to control costs based on activities rather than just Profit & Loss reports giving a single view of the story.

ABC assigns cost (through cost drivers) to activities based on their use of resources and assigns costs to cost objects, such as products or customers, based on their use of activities.



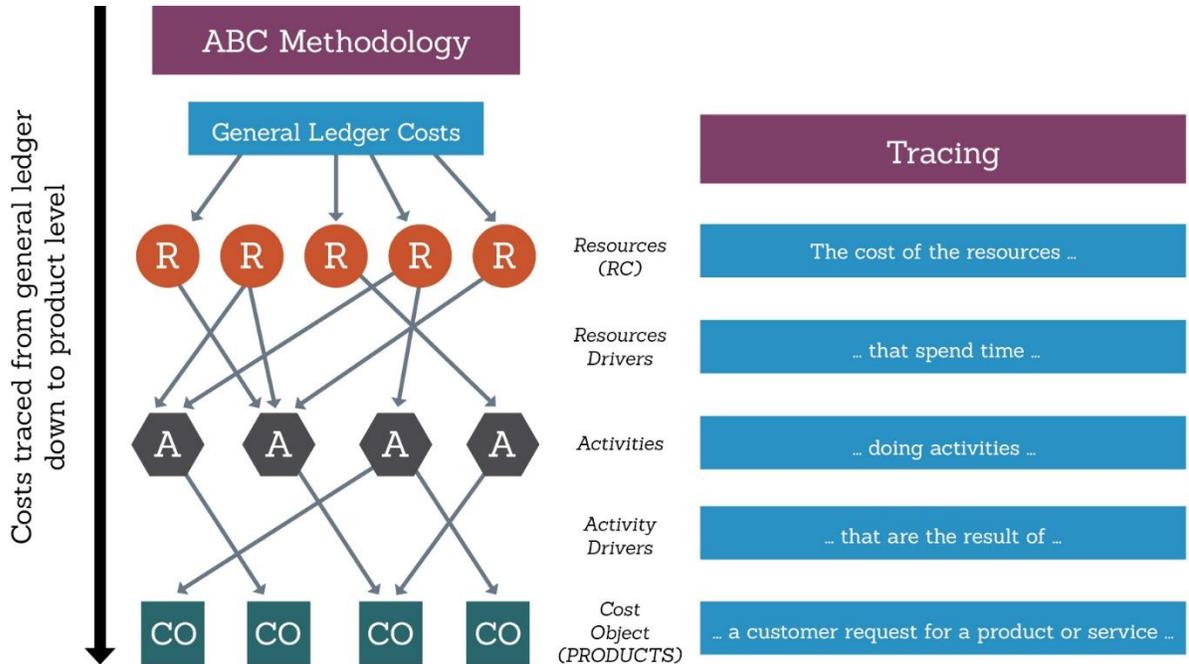
Your General Ledger (GL) will contain your costs and your first step is allocating those costs to resources supplied. You will then determine the activities and their costs based on resources used, and finally assign costs to products/services based on their share of activities.

Let's start by breaking it down to the Why, What and How Well for you.



The value of ABC/M comes from the output of Profit & Loss statement per product, per channel, per client, per time period, or any other business dimension.

The Vertical View of ABC: Five key segments that are clearly linked and follow a logical sequence



The danger in any ABC project is getting stuck in an agreement around what the Resources/Activities/Cost Objects are. An ABC project requires accurate data but don't, for example, get stuck asking employees to record timesheets to an exact degree to work out some driver values. Implementing ABC successfully is enabled by embracing the 80/20 rule i.e. its 20% of allocations that gives you 80% of the benefits. Don't sweat the small stuff but instead ensure you have strong stakeholder buy in to the ABC project to ensure you can push through the small stuff.



GL Items ranked	
Freight	46%
Staff	29%
Property	7%
Head Office support	5%
Warehouse	3%
Other costs	10%
Total	100%

- Customer Service
- Debtors Mgt
- Primary Financial Support
- Warehouse**
 - Receiving
 - Bulk Stacking
 - Normal Stacking
 - Picking - variable
 - Picking - fixed
 - Packing
 - Variable Forward Picking
 - Fixed Forward Picking
 - Variable Replenishment
 - Fixed Replenishment
 - Despatch
 - Storage
- Decoder Handling
- IT Operations
- Management

- 001 - Cost Centre 1
- 002 - Cost Centre 2
- 003 - Cost Centre 3
- 004 - Cost Centre 4
- 005 - Cost Centre 5
- 006 - Cost Centre 6
- 007 - Cost Centre 7
- 008 - Cost Centre 8
- 009 - Cost Centre 9
- 010 - Cost Centre 10
- 012 - Cost Centre 11
- 013 - Cost Centre 12
- 014 - Cost Centre 13
- 015 - Cost Centre 14
- 016 - Cost Centre 15
- 017 - Cost Centre 16
- 018 - Cost Centre 17
- 019 - Cost Centre 18
- 020 - Cost Centre 19
- 021 - Cost Centre 20
- 022 - Cost Centre 21
- 023 - Cost Centre 22
- 024 - Cost Centre 23
- 025 - Cost Centre 24

What are the key outcomes of successful ABC implementations?

- Fine-tune your strategy to improve profitability by optimising product or customer mix
- Providing a clear insight of where to control costs
- Changing organisation behavior with clear views and communication across Lines of Business

Every organisation whether a Manufacturer, University or Government Department can use ABC/M to great benefit. Most important is recognising that each organisation will have different Resources, Activities and Cost Objects, which makes it just about impossible to buy a package solution off the shelf.

To learn more how IBM Planning Analytics offers the best solution for ABC/M project, please download our next whitepaper: “Activity Based Costing Powered by IBM Planning Analytics”.

Written by

James Wakefield – Director of Solutions & Marketing - Tridant Pty Ltd

Rossouw Koegelenberg - Managing Director - Venn Cubed Pty Ltd

David Meadway – Practice Area Lead - Tridant Pty Ltd