

Undertaking an ABM project

Objectives of the project

Embarking on an ABM project is not a trivial exercise. Like any project that has to make a significant impact on business performance it will require dedicated resources, the co-operation of the business to become involved in the task of data collection, and the determination of the top team to use the results to improve the organisation's fortunes.

The success of using ABM comes when every function sees uses for the model outputs both from a functional perspective and from a process perspective for the business as a whole. The top team collectively should all be very interested in seeing product and customer profitability. Further, the outputs from the model need to be seen by everyone as the fundamental base of knowledge to make better decisions on the products or services portfolio, the mix of customers the company wishes to acquire and nurture and as the launch pad for significant process improvement.

Also, beware the 'ABM evangelists' surrounded by an auroral glow fresh from an ABM conference expounding loudly on the elegance of the analysis embodied in an ABM model. The end result may well be a model that is a benchmark in its own right, but without a real business purpose for creating it such a model will languish in a cupboard next to many other laudable projects that started with high hopes but ended without any measurable outcomes.

If the primary aim were profitability analysis then the initial model would generally start with a high level of activity analysis. However, for an Electricity Company for example, where the customer segmentation would be determined by the myriad of detailed processes created by customers, then the activity analysis is necessarily far more detailed.

If the aim of the model is to establish profitability first, followed by process improvement, then activity data needs to be detailed enough to pick up the failure activities and through attributes prepared in a way that readily allows process analysis by type of activity.

During any ABM project it is invariably the case that as the model starts to deliver new and significant insights about the business this prompts further questions to be asked. Not all such questions can be determined at the outset during the planning stage. In these situations the flexibility of ABM comes to the fore. At any stage, more detailed data collection can supplement any initial high level data. At any stage, where the model is deemed to be particularly sensitive to a range of cost drivers rather than the initial raw driver chosen, the activities and drivers can be modified. At any stage, if subtle insights can be obtained by further segmenting the customer categories, appropriate activity drivers can be found to assign activities to a more detailed level. The only discipline that must be followed rigidly is to keep the log of changes to the model completely up to date.

Key steps

The ABM process steps outlined here are generic. Care needs to be taken to ensure that for each ABM project, the specific steps to follow and the detailed content of each step are tailored to the needs of the company. The following check list of each step and the desired outcome is a useful guideline for most ABM projects.

Project start-up and detailed planning	
Establish Steering Group and Project Team. Confirm objectives.	<i>Project properly resourced and managed. Expectations agreed</i>
Provide thorough pre-project training in the principles and practice of ABM techniques.	<i>Role of the team and the ABM understood by the team</i>

Prepare and undertake briefing/ communications to senior managers	<i>Awareness of project, its aims, degree of staff involvement</i>
Define products, channels and customers to be costed.	<i>Scope of the analysis determined</i>
Assess characteristics of segmentation and availability of sources of data.	<i>Boundary of accuracy of analysis determined</i>
Preliminary identification of processes, activities and drivers	<i>Provisional list (or map) of processes</i>
Assess suitability of general ledgers for analysis and agree period	<i>Areas of risk identified and agreed with Steering Group</i>
Select systems to capture and model activity based data	<i>Systems requirement agreed and actioned. (and acquire software).</i>
Detailed work step planning	<i>Steering Group signs off plan</i>

Establish preliminary understanding of cost dynamics

In key areas, such as Sales, Customer Service, Production, etc., make field visits to understand the business.	<i>Project informed by a deep understanding of the work and the customer facing issues</i>
Outline process maps created	<i>'Helicopter' view of the business seen by team</i>

Activity and cost driver identification and activity quantification

Review organisation, processes, activities and cost drivers with managers.	<i>Dictionary of activities and cost drivers confirmed</i>
Identify sources of quantitative data for activities, cost drivers and cost driver variability	<i>Sources identified (such as current recorded data, need for interview, etc.)</i>
Capture time allocations to activities	<i>Basic data found</i>
Agree allocation of non-staff costs and other non-frontline costs	<i>Provisional costing model in paper schematic form</i>

Development of activity costs and their validation by managers

Agree basis of allocation of general ledger costs to activities (resource drivers)	<i>Resources to activities links established</i>
Classify activities by type and by process	<i>Basis for further analysis created</i>
Build first stage ABM model to reflect cost allocations and activity type and reconcile activity costs to general ledger	<i>Foundation of ABM model built</i>
Review activity costs with managers	<i>Buy-in by management to activity costs</i>

Cost driver volumes

Identify suitable sources of cost driver data for a suitable period and any surrogate drivers where necessary	<i>Refined cost driver dictionary</i>
Download or manually record as appropriate	<i>Basis for calculating activity cost per unit cost driver (output costing)</i>

Review with managers and compare volume variations with level of driven activities	<i>Management confidence in selection of cost drivers</i>
Where material, record cost driver variability	<i>An understanding of where to apply greater sensitivity to the ABM model</i>

Revenue data	
Capture revenue by product, channel, customer, and any other segment of interest	<i>Basis for product, channel and customer profitability created</i>
Download hard data via MIS or manually input	<i>Model loaded</i>
Review revenue data with managers	<i>Buy-in by managers</i>

Model building and validation	
Design final structure of model and agree principles with Steering Group	<i>Key principles agreed</i>
Build second stage of model and apply cost driver and revenue data	<i>Model structure resident on PC.</i>
Reconcile to general ledgers	<i>Logic check complete</i>
Review activity costs and output costs with department managers, and amend model as necessary.	<i>Buy-in by managers</i>

Analysis and interpretation of ABM model output	
Analysis by activity costs by activity, cost driver, process, product, channel and customer segments	<i>Insights into the activity structure of the business, its processes and cost drivers</i>
Analysis of product, channel and customer profitability	<i>Understanding of areas of profit erosion and profit opportunity</i>
Feedback to management of all analyses	<i>Buy-in by managers</i>
Development, with management, of changing strategies (discounts, margins, segments, etc) to impact profitability	<i>Comparison of 'what-if' scenarios</i>
Development, with managers, of improving processes to impact profitability	<i>Focus for management action</i>

Review of output from project and agreement of next steps	
Presentation to Steering Group and senior management of the complete model, its structure and the bases on which it has been developed. (assumptions and data capture period)	<i>Ownership of the ABM model by the board and recognition of the importance of model as a tool to assist the effective decision making within the business</i>
Presentation of significant findings, conclusions and recommendations, and discussion of the options available to improve overall profitability	<i>Management action plans that respond to the ABM information generated by the project. (customer retention, divestment & acquisition strategies, process-re-engineering, pricing policies, service levels, etc)</i>

Areas of potential difficulty

All projects have difficulties. In ABM, these are mainly concerned with data and the resources available to search for and supply it. Some of the difficulties encountered are:

1. The ease with which data will be available to segment the customer base.
2. The extent to which data contained within the general ledgers is appropriately structured to support product, channel and customer profitability analysis.
3. The extent to which it will be sensible to identify and quantify activities in a sample of the organisation and then extrapolate these to the whole of the organisation. This is particularly relevant where, say, a multi-regional structure appears to be consistent across the whole country.
4. The ease with which data can be extrapolated via current systems, and the degree to which this is up to date and accurate.
5. The ease with which data concerning cost drivers is available from existing records and that it is appropriate.
6. The staff needed to provide data on data collection forms, via interviews or workshops are available and knowledgeable.
7. A project team being available for the duration of the ABM project, preferably on a full time basis. They should also have the aptitude and skills to undertake the work. A core team is required for the duration of the project. The core team will have responsibility for building the actual ABM model. Members of the core team will become a 'centre-of-excellence' for ABM, once the main project has concluded its work. The core team may be extended into a larger team by including additional full or part-time members for the stages that involve data collection.

Software

ABM models can be built on spreadsheets, but only the very simplest of analysis can be undertaken. The creation of spreadsheets to handle the assignments of resources and activities soon creates a spreadsheet of vast complexity full of look up tables and multiple sheets, growing organically as the demands for more analysis are built in. The main disadvantage of spreadsheets is that they are rarely documented as they are built. Only the creator can remember, and then only vaguely, how it was all put together. Database tools have a lot of the functionality required to undertake ABM analysis but on their own still have gaps in undertaking all the necessary requirements of a model.

The best fit is obtained from using propriety ABM software. Such software is available, which is robust and easy to use and has been subjected to continuous development over at least ten years. The software has been designed to facilitate the building of large models of high complexity while at the same time making it easy to track the logic of the cost assignments. The software includes simple links to import and export data from and to other spreadsheet and database tools, as well as packages to present the output from analyses in graphical format. The key is to have powerful ABM software, managed by the ABM experts, with straightforward easy to assimilate outputs fed to any number of managers' desks where decisions are taken.

An ABM model requires a lot of fast processing power, but sufficient power is available on most desk-top PCs. In a team environment, each member can work on building parts of the model and entering activity and driver data on their own machine, periodically integrating the data on the main model via the team's network. The team should also have access to the company's transaction files.

Depending on the size of the business and the level of integration required in the longer term, the ABM model can be linked on a more permanent basis to the company's main systems and files. This may involve feeding from the normal transaction files or from and to a

datawarehouse. For geographically dispersed businesses, data feeds via the Internet can also be established. Proprietary ABM software keeps abreast of modern integration requirements.

Team resources

An ABM team should represent all the main functions within the business rather than be a team of financial specialists drawn from the finance function. The team needs to bring knowledge of the business into the project at the start to ensure that the data collection and analysis planning stage creates a series of project steps that will provide outputs that answer the key questions raised by the business.

Team members need to be credible individuals. They will be interacting with the rest of the business at all levels; gathering data, analysing outputs, drawing conclusions and making recommendations to the senior team. Once the ABM project is completed the model becomes a dynamic decision support tool. Most team members will return to the business while a nucleus continue to keep the model up to date and work with managers to extract the maximum value from the model. When ABM is part of business-as-usual, then ABM can be termed a success.

Use of Develin & Partners consultants

The use of our consultants to support an ABM project should follow the usual criteria for seeking outside help. We can also provide expert knowledge about the selection of appropriate software. Our role is to help steer the company during the planning and model building stages, speed implementation and avoid pitfalls.

Our consultants transfer skills and knowledge to the client team and build a centre-of-expertise among the company's team members. Further, we assist the process of embedding ABM in the company, both technically and to ensure ABM becomes a tool to provide daily support to managers.

When using consultants it is important not to put them in the position of building the model without any client team involvement at all.

Embedding and refreshing

Key measures of success of an ABM project are:

- the credibility and ownership that the inputs and results of the ABM model achieve among middle and senior management;
- the speed with which the project can be used to influence decision-making;
- the degree to which the project creates a self-sustaining centre of ABM expertise in the organisation capable of maintaining the use of ABM on an on-going basis
- the ABM implementation brings significant benefits to the business.

An important aspect of the ABM Project is the technical embedding of the methods employed so that future refreshes of data can be achieved quickly and with fewer resources. During the ABM project phase, data collection, particularly the collection of cost driver volumes, usually involves analysing a wide range of company systems' files from a number of sources. These analyses are normally completed 'off-line' within the team. Where possible, these analyses need to be automated so that the relevant data to refresh and update the model can be downloaded from the company's systems with little need for manual manipulation.

The initial model building is based on a number of assumptions concerning level of detail, relevance of certain cost types and so on. The initial approach tends to err on the side of caution in that too much detail finds its way into the model. During the project, the team will

have analysed the business in some depth and will be able to stand back to make a judgement on data relevance once the model has been created. With the knowledge gained during model build, and in conjunction with Business Managers, the team will be in a position to simplify the model in areas where such a change does not materially affect the outputs from the model. For example, there may be too many activities in a department, each costing very little. If done in partnership with Business Managers, the ownership of each part of the model will remain with line management.

The results from the first ABM model represent a snapshot of the organisation. Although there will be great interest in the output it will not be long before the results will diminish in impact as they are perceived to be dated. The model will need to be refreshed so it is up to date; a dynamic reflection of the current reality. The model has to remain credible if managers are to base critical decisions on the outputs.

A refresh of the model typically needs to capture the following:

- Actual costs or forecasts that are recent
- The latest driver quantities.
- Changes to the most significant activities in the model, particularly if process re-engineering has already started.

In addition to providing new information to the organisation a refresh will help to speed the embedding process and raise the capability of the ABM team to maintain the use of ABM for the foreseeable future.

Using ABM outputs for performance improvement

ABM model outputs provide the basis for performance improvement by Business Managers. In order to make this work and fuel the demand for ABM to be used:

1. Business Managers, Team leaders and Supervisors should be provided with information highly relevant to their needs.
2. The users must have the capability to use ABM information and be able to demand information from the ABM team.
3. The users must have an understanding of how their own function interacts with others and how to use ABM information as the catalyst and vehicle to hold meaningful dialogues focused on improvements to unit costs and customer service.
4. The ABM Team and both Process Change Managers and ISD teams need to work together with complimentary skills and appropriate frameworks.

In order to drive the supply of information to meet the demand:

1. The ABM team has to be capable of refreshing the model at appropriate frequencies as governed by regular reviews of what within the model is relevant.
2. The collection of all data will have to be automated as far as possible.
3. Business Managers and others must be willing to collect certain data on an on-going basis.
4. A close relationship should be developed between the ABM Team and other groups who support change and record the effects, such as Process Change Managers.

An ABM team is ideally placed to help users of ABM data to understand how the different functions interact and therefore allow meaningful dialogue across functions focused on improving unit costs and customer service. The first task is to structure the data into a highly visible and usable form based on the notion of event triggers and cascades of activities. The key stages are:

1. The team brainstorms key events (both business and customer related) and construct the activity cascades (processes) for the core process and all the branches off it that represent failures either internal or customer induced.
2. The team structure output data from the model to reflect the different events, the cascade of activities, cost driver volumes, and both total and unit costs.

The team are then be in a position to advise Business Managers of the multifunction activity cascades within the ABM data and all the interactions and interdependencies. Where Business Managers believe that there could be several significant cross functional issues to be resolved, the ABM team embark upon a more pro-active initiative involving the following steps:

1. Facilitate multifunctional groups of managers in identifying key opportunities to influence unit costs, reduce cycle times and or influence the behaviour of customers.
2. Set up mechanisms to put improvements in place.
3. Facilitate the groups of managers in identifying measures at appropriate points in the activity cascade and set up reports at appropriate frequencies. These form the basis of a set Key Performance Indicators.

Using ABM for commercial decision support

Business process management is about improvement; better efficiency and effectiveness. Commercial management is concerned with portfolio, pricing and margin management decisions.

These decisions are concerned with:

- The range of products or services the company wishes to offer
- The types of customers it wishes to trade with
- Making products in-house or using sub-contractors

If we needed to know the impact of reducing the product range, or changing the mix of customers, or deciding to use sub-contractors for some of the work, then it is key to be able to trace the potential decision through to the activities in the organisation. We can only know the costs that are then avoided if we can trace the costs. Without this knowledge, portfolio decisions would be based on best estimates of the impact, or worse, not recognising the true level of avoidable costs and thus keeping them.

The ABM analysis provides the means to perform customer engineering, by answering basic questions, such as:

- Which are the least profitable customers and how can we improve their level of profitability?
- How can we protect the relationship with our most profitable customers?
- How can we re-direct the salesforce's efforts away from going for volume towards going for profit?
- Is it more profitable to re-direct low volume customers through wholesalers, rather than servicing them direct?
- Should we have a segmented discount structure based on customer attributes relating to service level needs, rather than on total volume supplied?
- What will be the impact of introducing an 'e' channel to customers via the web site?

Product and customer profitability analysis provides the basis on which to determine the product and customer portfolio. Those customers having a negative contribution would immediately draw attention to themselves. If the volumes were low and there was little chance of increasing the contribution then they may become candidates for elimination. The danger with such customers is that sales volumes could increase, further dragging down overall company profitability. Problem customers have healthy volumes but low profitability. These require more detailed study to see if the mix of products is the cause of the problem. Action on selective product pricing might then make the account leap in profitability.

Customers having potential are those where higher volume sales add significantly to overall company profit. Any action on price and volume further positively impact profit, although care should be taken as such customers are valuable to retain.

For any one customer, a product profitability profile shows if there are any products that are significantly lowering the profitability. Actions to change product prices to the customer are difficult to put in place. A unilateral decision to cut out certain products would be unwise; the customer may transfer all the profitable products to a competitor.

The key to using ABM profitability data is not to take instant action to eliminate any negative products or customers but to make a measured review of the whole relationship to customers. There could well exist a strategic reason for continuing in some unprofitable relationships. This may be a short-term position while a market presence is being built up, or it may be to keep the competitors out of segment in one area where the products and customers are profitable in all other areas.

The power of using ABM outputs is that managers know the consequences of making decisions rather than wait for an indeterminate result to appear when it is too late to redress a poor decision.