

# up a notch<sup>TM</sup>

## Improving the measurement of financial performance



### Hide & seek financial measurement

The principles of financial statement construction were taught to MBA students long before President Eisenhower left office. The conventional wisdom is that large corporations certainly must comply with those well-known principles. Not so. Based on observations gathered over two decades of Unbeaten Path consulting experiences, comprehensive compliance is the exception to the rule. Here's a sample of the kinds of scenarios we typically encounter:

- ❖ Chart of account structures that have survived from pre-computer days (amazing consequence: new account numbers are now assigned more or less at random because there's no more room to "squeeze" them into what used to be the "right" place)
- ❖ Overhead costs and labor costs added to all BOMs as two universally-applied part numbers
- ❖ No cost of sales variance reporting (at all)
- ❖ Foreign exchange gains/losses on raw material purchases ... and ... cash discounts earned on early payment of raw material invoices mixed with purchase price variance reporting above gross margin
- ❖ Wild guesses on balance sheet reserves for inventory obsolescence
- ❖ Balance sheet valuation of inventory includes labor + burden absorption held in "scrap" part numbers pending a "regrind" process.
- ❖ No measurement of the distinction between sales at list and gross sales
- ❖ Frantic last-day-of-the-month shipping on the overtime clock to customers that don't want the merchandise yet
- ❖ Sales returns not shown separately from gross sales
- ❖ Professional service expenses for marketing (decided on at HQ) co-mingled with manufacturing cost of sales measured at the plant 2,000 miles away
- ❖ Functional marketing expenses (e.g. wages) mixed with advertising distribution costs
- ❖ Cash advances to managers not indexed for inflation in hyperinflationary environments

External auditors don't complain about these kinds of things because they aren't "material." With the exception of items with balance sheet involvement, they don't effect bottom line profit ...and even the balance sheet involvement items get smoothed out over a multiple year horizon.

### The opportunity cost of imprecision

The auditors may not object, but the cost of imprecise financial measurement is very large. It allows the corporation to under-perform. Here are some opportunity cost illustrations:

Senior managers don't notice distinctions vis-a-vis world class performance. Cost saving issues never end up on the table for discussion. Product pricing isn't efficient and/or items that are losing money aren't rationalized. Salespersons don't act like they are business managers. Management performance bonuses are based in part on results outside of the control of the measured individual.

## Overcoming barriers to change

Fixing these things isn't easy because there's typically a tremendous amount of inertia when change is suggested. That's universally true but even harder to overcome in the financial area.

One manufacturer in Illinois decided it was less work to continue to struggle looking for randomly-assigned/out-of-sequence G/L account numbers than it was to start over with a restructured chart of accounts based upon a hierarchical format. They kept an IS guy busy the entire budget season looking for FRS "account missing" errors that would have been permanently solved with wild card functionality off a hierarchical chart.

Milt Habeck, Unbeaten Path's founder, is a disciple of precision financial measurement because he saw it thrive first-hand in enormously challenging hyperinflationary environments. Two medium-sized companies (one in Buenos Aires and one in Rio) embraced the vision and then those companies started making profits and generating robust cash flow for the first time in several decades. Please click/review these two persuasive testimonials: [Argentina](#) [Brazil](#)

Click [here](#) to see information about a one-day course that introduces the art of managing manufacturing enterprises in overseas environments.

## Unbeaten Path can help your company

If you are looking for seasoned, internationally-savvy, practical advice for moving your company towards higher profits, please consider contacting us. A "**No Stone Unturned**" operational assessment performed by Milt Habeck would deliver valuable strategic insights and a prioritized plan to start moving the bottom line up. You might find these two links interesting:

- ❖ Professional profile for [Milt Habeck](#)
- ❖ Parts & pieces of a "**world-class**" P+L specimen

## Questions ?

It would be a privilege to answer any questions about our "**up a notch**" consulting services. Here's Unbeaten Path International's contact information:

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