Profitability simulations

Article 4:
Simulating profitability numbers for clients, products, processes, business segments and across the overall business

Management summary

Fourth in a series of articles on the topic of “Smart” client and product profitability. This article focuses on financial simulations and new – Nov19 release - functionalities in Axis

Key messages

- Assess impacts of business decisions on future profitability
- Early identify areas that could hinder success of products or business lines
- Monitor progress against plan

Fore-warned is to be fore-armed

www.axis-analytics.ch

Simulations, in this context, can be summarised as:
Assessing the impacts, financial and otherwise, of intended business decisions

The process of producing financial simulations forces the user to go through a more detailed set of assumptions together with substantive reasoning of the drivers and impacts. As with any business decisions, **proper preparation avoids pitfalls later**.

This article focuses on financial simulations in relation to:

- Launching new businesses, product lines or even individual client relationships
- Introducing major changes within a business
- Build or buy decisions, especially offshoring, outsourcing and, also, insourcing
- Assessing changes designed to improve efficiency
- Business planning and budgeting

Practicalities of generating simulations

It would be Nirvana if every business proposal included a solid, relevant and dependable financial simulation. Accounting ledgers are primarily designed to provide outputs for statutory reporting and less for management analytics. With the limited format of accounting data outputs, financial simulations are often produced at a summary level and use, in the main, broad assumptions, thereby limiting their reliability and dependability.

This results in business managers extracting portions of data and numbers from different sources to arrive at more meaningful financial simulations, often including some sort of process costing. A common challenge seen in many executive discussions is the lack of proper reconciliation between accounting data from the booking ledgers and financial simulations justifying business proposals. Readers will recall hearing the statement from the CFO: “These are not my numbers!”

Any additional information that assists getting a proper link between accounting ledger data and financial simulations at various levels provides much more comfort and reliability and is invaluable to any business.

Financial simulations in Axis

A November 2019 update to the Axis tool greatly expands the profitability simulations capabilities allowing managers to assess the financial impacts of intended actions, thereby enabling early identification of potential hurdles and hence, their in-time remediation

An underlying feature is the availability of globally consistent, detailed profitability statements by client and/or product across the whole business, thereby providing actionable indicators for any remediation requirements.

Article 2 in this series already covered the basics on Individual client relationship and product profitability simulations. A brief recap:

By comparing with a similar or average client relationship or product:

- Assess the financial outcome of new client relationships or products
- Identify specific work processes that result in unduly high costs
- Implement required remediations
- Measure the resulting success

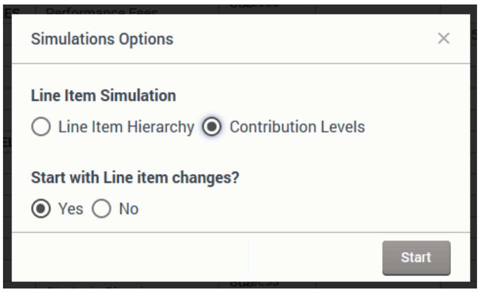
The November 2019 release of Axis takes simulations to the next level, now including:

- Simulating profitability for business segments, processes and the overall business
- Bulk updates of cost lines using percentages and/or absolute changes
- Results both in work process and accounting lines formats
- Assessing marginal revenues and costs

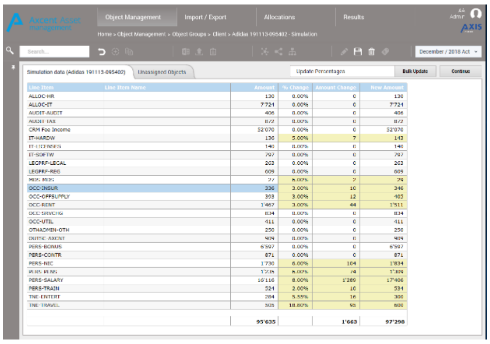
This new functionality can also be extended to include preparation of the annual financial budgets and business plans.

Overview: financial simulations in Axis:

1. For individual products / clients, work processes, business areas, overall business
2. At both booking line items (Chart of Accounts) and also work process levels

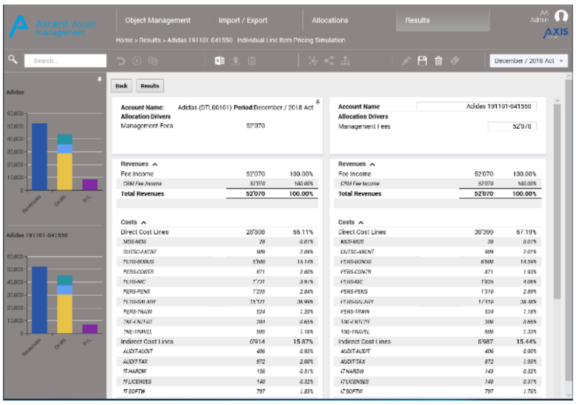


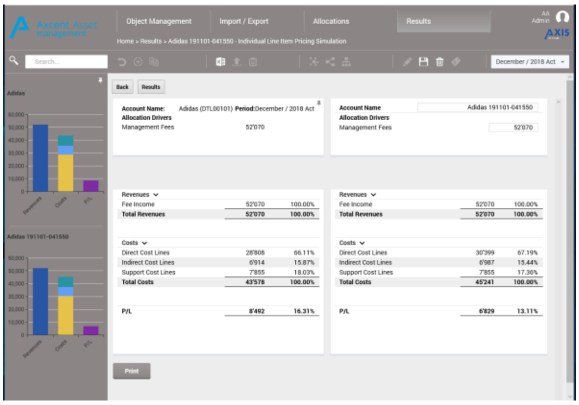
Step 1: After selecting the dimension (individual product / client, work process, business area / region or overall business), choose whether to start with line item changes or using work process costs.



Step 2: Assess what revenue and cost lines would change and by how much. As input, by line item, use percentage changes to drive the result or absolute numbers and let the percentage change be calculated. Especially relevant for marginal costing

Step 3: Continuing after making the line item changes allows user to see the results, both in detail and summarised by major revenue and cost types





All outputs visible on screens above can be downloaded into MS Excel for both any further analyses and inclusion in other reports.

Summary:

- Performing financial simulations forces the user to dig deeper into potential impacts and then attempt to quantify them
- Senior management also feels more comfortable making business decisions knowing that solid preparatory work has been undertaken that justifies the decisions
- Enabling such financial simulations is key to any financial analytics tool

Authors:

Paresh Sodha, Managing Partner at Axcent AG in Zurich. Prior to joining Axcent AG, Paresh was, for over 15 years, the CFO of a large global asset manager, having first-hand experience of implementing smart client and product profitability tools.

Thomas Völke, Partner at Axcent AG in Zurich. Thomas has over 30 years experience in project management involving Finance and Operations teams and more recently, leading and driving product & client profitability analytics within financial industries. He has now brought this experience to the team developing AXIS as a strategic Profitability Framework and Financial Management instrument.