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Boise State on Business: Companies Must Balance Feelings and Facts

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BOISE STATE ON BUSINESS

Companies must balance business feelings and facts

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Many companies are founded with innovation, enthusiasm and hopes for success. In its inaugural days, the business founder/CEO is able to personally drive the company's success with a passion while wearing multiple hats and controlling all aspects of the business operations. They understand their market, can effectively communicate their chosen mission to employees and have a good "feel" for their cost and margins.

However, there comes a point where sales grow, new employees are hired and operations expand. All of a sudden, it becomes evident that managing by "feel" is not enough. Founders/CEOs must transition from managing by "feel" to managing by facts as they become accountable for business direction.

Management by facts requires formal accounting tools to answer key business questions: What are the costs of the business's products? How much should the business sell to break even?

My students and I conducted "learning in action" projects that show that job costing, activity-based costing/management and margin analysis are the minimum requirements for new companies. These formal accounting systems provide the hard facts that allow new companies to understand and manage their costs and margins. These systems provide the factual support for the passion that founders/CEOs use in creating each new company, and to balance management by "feel" with fact.

Unfortunately, many new companies have not prioritized the proper design and implementation of these formal accounting systems. This process leads to the current high failure rates of new companies.

New companies that survive beyond early failure are said to enter into a maturity phase. These companies have robust costing systems to ensure that their targeted costs and sales volumes are achieved. However, this also creates a problem for mature companies. Since CEOs become absorbed with facts and meeting cost targets, many mature companies channel resources into prioritizing cost reductions and competing on price.

While this behavior provides some certainty to improving profits, it comes at the expense of the "feel" that is the innovation, enthusiasm and passion that created them in the first place. Primary examples include Apple, Blackberry, Dell and HP. These companies are in what has often been termed a "maturity crisis."

Our projects suggest that CEOs must use these established accounting systems in new ways to overcome a maturity crisis, and to bring back the "feel" that was once behind the innovation, enthusiasm and passion at the beginning. Rather than focusing on cost reduction initiatives to meet targets, we suggest CEOs use formal accounting tools for identifying strategic opportunities with a view of renewal toward long-term prosperity. This can only happen if there are open roundtable discussions between managers and employees about the accounting information.

Instead of routinely examining variances in materials, labor and overhead costs, have instinctive discussions about these costs. For instance, if the cost of a product does not meet its target, CEOs and employees should throw around ideas about why that might be. If the company is a cost leader, perhaps it's time that employees explore new materials, or get a feel for new technological processes and infrastructure that may provide permanent reductions in all costs. If a company is a product leader and innovator, perhaps it is time to tap into the development pipeline to launch the next new product at a given cost, and reap the margins of premium pricing from early adopters.

Mature companies need to keep their employees talking about new possibilities. Meet face-to-face and engage in regular open discussions. These are simple but crucial steps in balancing management by fact with management by "feel."

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