Finance effectiveness benchmark study 2010

Is finance rising to the challenge?

Contents

Foreword

PricewaterhouseCoopers provides benchmark assessments of the finance functions of a range of leading international firms. Companies can then identify improvement opportunities and formulate a plan to realise them.

Against the background of gradual economic recovery, ‘Is finance rising to the challenge?’ outlines the latest findings from the benchmark analysis of over 100 participating companies. In particular, the report examines whether finance teams are equipped to provide the levels of strategic insight, risk oversight and other key aspects of the ‘business partnering’ role now expected by many CEOs. It also looks at how the best performing finance functions (those in the top quartile of benchmark evaluation ratings) are able to meet evolving business needs, balance being a business partner with their traditional responsibilities and ultimately deliver real value to the enterprise.

What comes through clearly from the findings is that while considerably more finance functions now regard themselves as true business partners compared to a year ago, many organisations still lack the necessary capacity and capabilities to fulfil this role. There is also strong dissatisfaction with the quality of management information, especially forward-looking analysis that enables firms to stay ahead in a fast-changing and competitive environment.

We compare performance both between internal business units or divisions, and versus a relevant group of peer organisations. The results enable companies to assess the size, shape and nature of their finance function, and the ability of the function to deliver the needs of the business. The benchmark can be used to chart progress and sustain momentum (for more details about the benchmark evaluation please see page 15).

If you would like to assess the performance of your finance function or discuss any of the issues raised in this report, please contact your usual PricewaterhouseCoopers representative or visit www.pwc.com/ie

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The report is based on the benchmark analysis of over 100 leading companies, comprising over 1700 discrete businesses, in 60 countries. The assessments were carried out between September 2008 and November 2009.

Executive summary

CFOs and their teams are struggling with the increasing and competing demands placed upon them, particularly coming out of the downturn. Finance functions, focused for so long on compliance and control, have found themselves under great pressure to tightly manage costs and provide more and better management information to the business.

CFOs are juggling to achieve the right balance between three competing agendas; insight, efficiency, and compliance and control – in addition to managing and motivating their people. They want to ensure the way they are steering the function and partnering the business is building towards a high performing function and one which is recognised as integral to success.

The need for finance to act as a true business partner has been thrown into sharp relief by the global recession and the heat is now on to demonstrate its ability to add value above and beyond its traditional responsibilities. However, when it comes to business partnering, our analysis indicates finance's ambitions often outrun its abilities.

PwC's benchmark findings in 2009 show 63% of finance functions are playing a lead role in the strategic planning process – acting primarily as facilitators or as a support for the CEO – this is against 54% in the previous year. Yet as the evidence in this report shows, little has changed in terms of the underlying behaviours or capabilities of the function. Does this increase represent genuine progress or does finance merely believe it has changed when it has not?

It is clear in many cases finance is struggling to meet expectations; either because of a shortage of the right skills or under-investment in the necessary tools and infrastructure. As the economy recovers, finance's ability to deliver on the promise of business partnership will be critical in its ability to navigate through the tough new competitive, investment and regulatory landscape that recovery is likely to bring with it.

Finance functions which can rise to this challenge will play a pivotal role in enabling businesses to capitalise on unfolding opportunities and build a platform for long-term profitability and growth.

Business partnering defined

Business partners are finance employees with the skills and experience to work alongside the business; influencing, designing and executing business strategy and planning. Business partnering requires the ability to understand both finance and business realities, to challenge decisions and, in many ways, act as a business consultant.

Insight

The study raises concerns about whether most finance teams are equipped to deliver the kind of support CEOs are demanding. While engagement in insight activity has increased, the actual number of Full Time Equivalents (FTEs) in business partnering roles has barely changed since 2008 (up 1% to 11%). When set against the widespread dissatisfaction with management information (see below) and limited evidence of any increased investment in this area, this suggests even though some additional staff are being re-assigned to partnering activities, they may not have the training, resources and business acumen to ensure their input is of real value to the business.

In addition, more than 80% of participants are dissatisfied with the quality of management information (MI). Particular concerns centre on whether the MI is sufficiently meaningful and forward-looking to drive business decisions in an increasingly complex and uncertain business environment. Underlying difficulties include broadening the focus of MI to provide sufficient breadth of non-financial performance data and being able to develop timely, reliable and comparable metrics for such information.

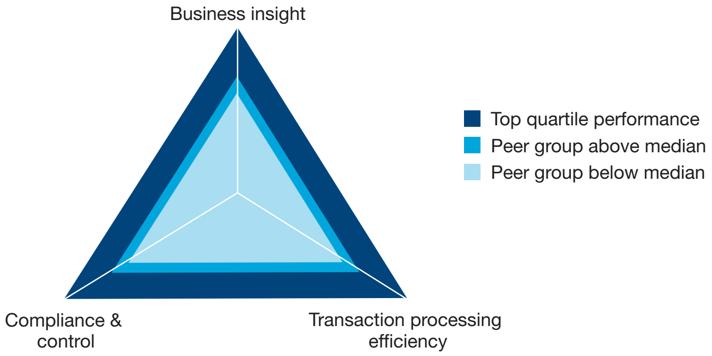
Efficiency

Streamlining operations and standardising processes continue to be high on the finance agenda as finance functions seek to reduce costs, enhance efficiency and free up more time for insight and analysis. Around 65% of companies benchmarked have consolidated at least some of their transaction processes. The more mature organisations are now looking to extend this approach to activities further up the value chain such as financial reporting and project accounting. However, the benefits of such moves are not necessarily being fully realised as processes have often not been rigorously standardised or simplified.

Compliance and control

At times of business change, it is essential to focus on the control implications of this change and the new financial, operational and compliance risks it brings. By doing so, the reorganised processes are more resilient and sustainable. Leading organisations have, despite the downturn, managed to make the move from the direct delivery of core transactional and risk management processes to more of a policy and oversight role, which enables them to manage the many changes impacting the business more effectively.

Figure 1: Competing demands



What sets top performers apart?

Participants in the top quartile of benchmark evaluation ratings are able to operate at much lower cost (top quartile functions operate at approximately 50% of the cost of the median), while sustaining high levels of insight, efficiency, compliance and control. A number of key attributes set these top performers apart:

- Clear focus on providing business insight (as defined on page 6), with top performers reporting a greater proportion of FTEs engaged in insight activity (30% more than the typical (median) finance function)
- Greater investment in business partnering capabilities (includes paying staff engaged in insight activity almost 25% more than the typical finance function)
- Better use of high value specialists' time achieved through standardisation of data models across markets and within business units and investment in sophisticated business information and analytical tools
- Combining financial and non-financial MI and developing simple and transparent metrics to align financial performance with the delivery of strategic objectives
- Transferring much of the routine transactional activity to consolidated service centres and achieving faster close times through active standardisation and simplification
- Strategic approach to cost management that distinguishes savings opportunities from spending that is needed to sustain the delivery of business objectives.

Into the frontline: the changing role of finance

Boards are looking to their finance functions to provide more active input into decision-making. In practice, however, it is not always clear how finance functions should fulfil this business partnering role.

All participants agree effective MI is the cornerstone of business performance management and governance, both in terms of risk management and planning for growth, and that finance has a key role to play in its delivery. Today, finance is increasingly active in the formulation and direction of strategy. 63% of participants in our benchmark assessments now regard their finance function as primarily a support group for the CEO or a facilitator of the strategic planning process, compared to 54% in 2008 (see Figure 2). The corollary of course is a third of finance organisations are still perceived to play a reactive and reporting-focused role.

When it comes to top quartile performers, the positive shift is especially marked with the proportion of insight FTEs, reported at 30% higher than the typical finance function (see Figure 3). These high performing organisations often deploy their finance people in business units with dual reporting lines, to the business and finance, while much of the transactional activity is transferred into consolidated group operations. This allows their insight FTEs to devote more time to analysis and other value adding activities and build deeper relationships with the business.

> ‘Considering the economic challenges we are facing, the key improvement that is needed is faster information, with more depth of analysis comparing us to the outside world.’
>
> CEO, oil and gas sector

Figure 2: Role of finance

Evolution not revolution

However, being a relatively new concept, there is no template for being a valued business partner or how this role should sit alongside more traditional responsibilities. A key challenge is how to strike the right balance between the potentially conflicting demands of strategic insight and independent oversight.

Back to basics

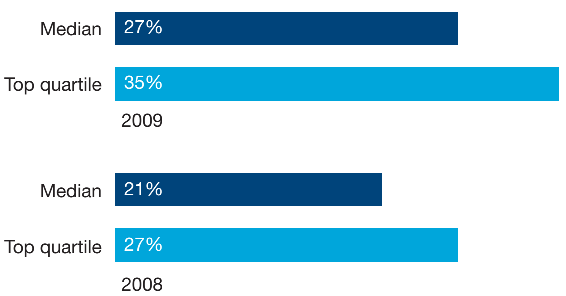
More than 80% of participants cite cost control as a key priority. However, there is an increased appreciation among top performers of the need to avoid arbitrary and unsustainable cost cutting programmes. With its organisation-wide view of expense, risk and profitability, the finance function is seen as being well-placed to raise awareness about cost and revenue drivers and identify opportunities for lasting savings.

Many finance professionals have dusted off their copies of Kaplan's texts to focus their thinking around cost control, as well as refreshing their knowledge of value drivers. However, many are finding the data is difficult to source and includes varying definitions (see page 10 for more information).

Business insight defined

Business insight is a key objective for most finance functions and entails effective partnering with the business to create value. Delivering relevant and timely management information and supporting the corporate performance management model are key priorities. In PwC's benchmark assessment, business insight activity is defined as comprising the following sub-processes: strategy and planning, budgeting and forecasting, management reporting, business analysis and performance improvement projects.

Figure 3: Percentage of finance FTEs engaged in insight activity



Organisations are also looking to senior finance executives to help strengthen oversight, co-operation and accountability across functions and geographical boundaries and ensure cost control initiatives are implemented successfully and in line with their overall business objectives.

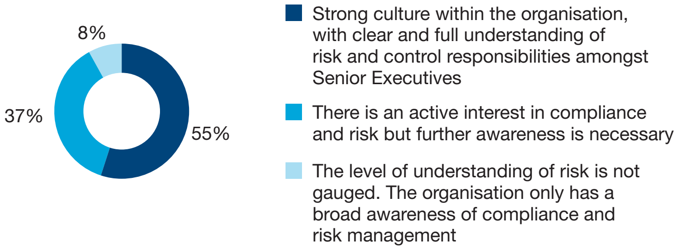
Oversight and control

Most finance teams we have studied have now overcome the initial challenges of establishing the policy frameworks required to handle current regulatory and related risk management requirements. However, performance in fully embedding these frameworks remains patchy.

Those finance teams that have achieved this are in a much stronger position to safely reduce the cost and compliance burden. Our research shows just over half the companies benchmarked reported a strong risk culture within their organisation, with clear and full understanding of risk and control responsibilities amongst senior executives (see Figure 4). Financial Services, however, will face new challenges as the regulatory landscape continues to evolve as a result of the downturn.

Having helped to raise risk awareness across the business, those finance teams are now shifting their focus to ensuring accountability across different functions and territories through enhanced risk analysis and exception reporting. Leading organisations are also moving from the direct delivery of core transactional and risk management processes to a policy and oversight role, with the day-to-day work being transferred to multi-functional group service centres (see page 12 for more on increased consolidation and use of shared services).

Figure 4: Risk culture and awareness



Up to the job: skills and capabilities

Simply re-assigning finance personnel to analytical activities may not be enough to meet business needs. As top performers recognise, the ability to provide real strategic insight demands dedicated resources, engagement skills and commercial understanding, as well as financial qualifications.

Although the proportion of finance FTEs dedicated to business insight activity has increased since our initial study, those engaged in business partnering roles has gone up by only 1% since 2008 (see Figure 5), suggesting many of the resources assigned to insight activity are not necessarily fulfilling the role of business partners. This is borne out by the fact most financial analysts still spend more time on data gathering than actual analysis (see Figure 6). By contrast, the opposite is true for the top performers, where nearly 60% of time is spent on analysis and insight.

Rising expectations

What management expects of finance teams is also expanding. This includes experience of managing change, the customer-focused mindset of a Shared Service Centre (SSC) and the engagement skills to work in collaboration with the business.

As more transactional activity is consolidated or outsourced, many finance teams also need the relationship management expertise to oversee contract delivery. More than half of participants have assigned business partners to manage transactional services, compared with less than 30% in 2008.

Bridging the gap

Recognising that simply re-labelling inexperienced personnel as analysts is not enough, top quartile performers are investing more in training and rewards. This includes paying an average of 25% more for staff engaged in insight activity than the typical finance function (see Figure 7).

However, the curbs on recruitment that have affected many finance functions during the recession have made it more difficult to bring in people with the necessary skills. While

Figure 5: Percentage of finance FTEs in business partnering roles

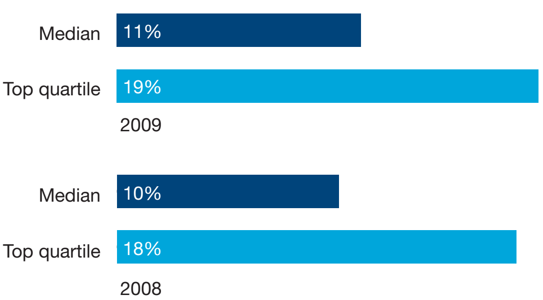
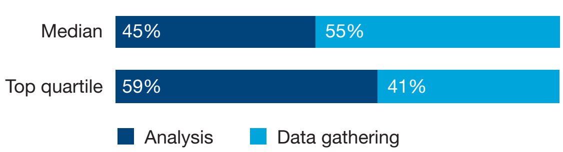


Figure 6: Percentage of analyst time spent on data gathering versus analysis



some participants are now beginning to resume selective hiring, budgets remain tight. Experience indicates a strategic approach to talent management that aligns recruitment, training and retention policies with long-term functional objectives can help to ensure limited resources are targeted most effectively. Many of the better performing participants also place greater emphasis on nurturing talent from within through rigorous succession plans for key roles and career maps involving secondments, specialist training in finance academies and job rotation across different business and support functions.

What gets paid gets done

Many participants are adjusting their approach to compensation to help promote the changes in culture that are likely to be required in a more demanding business and regulatory environment. This includes aligning more of their performance-related pay to risk-adjusted measures. Forward-looking participants are also seeking to align rewards with changes in strategy and desired behaviour through the development of balanced scorecards and a more appropriate balance between financial and non-financial performance indicators.

> ‘We need to improve our analysis to help the business drive the top line.’
>
> CEO, media sector

Figure 7: Average remuneration per Insight FTE (US$000)

Looking ahead:
more proactive management information

Management is demanding more incisive and proactive MI in a fraction of the time. Taking control of organisation-wide data management, non-financial as well as financial, often greatly improves the finance function's ability to deliver.

More than 80% of participants are dissatisfied with the quality of their MI, as Figure 8 shows. Dissatisfaction is greatest among group-based senior executives, reflecting the problems of sourcing consistent and comparable information from disparate business units. Many board members also complain their MI is slow to arrive and lacks the precision and forward-looking perspectives needed to inform decision-making.

Finance functions are being stretched by the demands of both gathering and, increasingly, also leveraging MI. Underlying problems include overly long and often ineffective turnaround cycles. Despite the significant amount of time devoted to planning and forecasting (see Figure 9), satisfaction with the quality of MI coming out of these activities remains low. Reasons for this include; a lack of clear definition from the business as to requirements, data not being structured to provide comparability, and inadequate tools, processes and skills to manage the activities effectively.

As outlined earlier, many finance functions are short of people with the necessary capabilities to translate reams of data into meaningful insights. As boards demand more non-financial metrics, finance also faces the challenge of sourcing, aggregating, assessing and interpreting an often unfamiliar array of information from across the enterprise. It is notable that while 46% of participants draw financial data from a central repository, only 23% can access non-financial and management reporting data from a common source (see Figure 10).

These challenges are likely to be heightened by growing statutory disclosure requirements. With climate change firmly on the global political agenda, and regulatory reporting such as the EU Emissions Trading Scheme, the Carbon Reduction Commitment in the UK and mandatory greenhouse gas emissions reporting in the US under the Clean Air Act, the need for companies to produce robust sustainability and climate change information is increasing.

Taking control of data

Bringing control of data management under one roof could help to overcome these challenges. While acknowledging that accountability for data, especially non-financial data, should continue to reside

Figure 8: Quality of management information

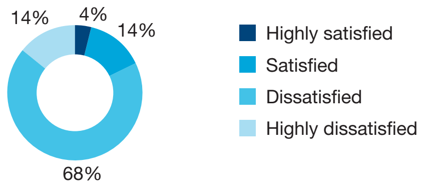


Figure 9: Percentage of time spent on activities

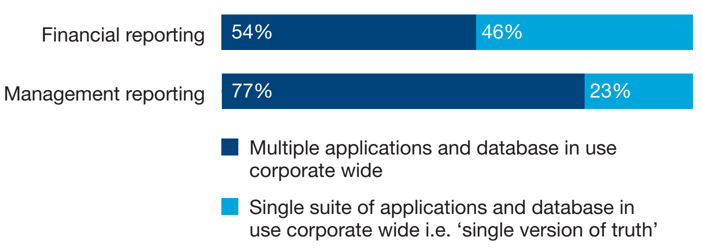
within the business, most participants believe finance is well-placed to act as the clearing-house for all information. Consolidation would enable finance to apply rigorous controls, processes and systems to cover all the diverse sources of information and promote a dialogue with the business about what MI is required to support management decisions. It would also allow finance teams to combine the results into meaningful performance analysis that can be clearly linked to strategic objectives.

The additional benefit of consolidation is the opportunity to standardise and simplify the data management process. It is notable most top quartile performers combine financial and non-financial MI in a single report and, partly as a result, spend far less time on data gathering and the associated challenges of data integrity and cleaning. In seeking to consolidate MI many companies have to consider further investment in data warehousing, ERP and other technology and processes that could help to facilitate more effective information supply and control. For some, the next stage is transferring data management to a Shared Service Centre (SSC), enabling them to release resources to focus on insight. These corporate data management functions often sit outside of finance, typically in group services or group operations, with finance retaining responsibility to set direction and policy. By adopting a consolidated, cross-functional model, these organisations have been able to overcome disparate ‘data silos’ and establish clear accountability for corporate data.

Creating meaningful metrics

The ultimate aim is the creation of a single version of the truth capable of providing a timely, relevant and reliable basis for decision-making. Finance now plays a crucial role in driving strategic execution by providing line management with the key performance analysis and indicators upon which to base their decisions and assess progress. Ideally, these metrics should provide a way to translate overall business objectives and the language of shareholder value into tangible guidance for people on the ground. Transparency is critical. Successful organisations are also adept at keeping their metrics as simple as possible.

Figure 10: Single enterprise database suite to satisfy reporting requirements



> ‘There is very little insight provided, and little value-add. If I ask for comment or pose questions, they are answered reactively.’
>
> CEO, financial services sector

Paying dividends: standardisation and simplification

With the direct costs of top quartile functions running at around half of those in median organisations, there is much to be gained through performance improvement.

Finance functions are under pressure to reduce costs. For many, this has included redundancies. However, without a parallel move to simplify the business structure and standardise processes, such cuts can often prove to be a false economy. Poorly focused redundancies can be especially problematic in firms that are heavily reliant on manual processes as they can greatly heighten the susceptibility to operational risk.

The most forward-looking functions are going beyond tactical cost-cutting. They are re-investing some of their cost savings to strengthen higher value areas such as business analysis and forecasting. Importantly, they are using the spending pressures as a catalyst to drive progressive changes that may have previously faced too much resistance within the organisation.

Greater automation could help to speed up processes, eliminate manual errors and reduce operational risks, while allowing finance professionals to devote more time to value-added roles.

Consolidation can also help to reduce cycle times and ensure key performance drivers such as cash flows are more visible.

Our benchmark assessment reveals the consolidation of finance processes into SSCs is gathering pace. Around 65% of participants have established SSCs or consolidated some element of their transaction processing, compared to around 50% in 2008 (see Figure 11). But scope and maturity varies significantly amongst participants. Less than 40% of the participants reported having a discrete SSC organisation that operates independently with a clearly defined governance structure and service level agreements.

Although less than 20% of participants are using SSCs for more complex activities such as financial reporting or project accounting, many have projects underway to identify activities higher up the value chain that could be centralised without compromising security, independence and control.

Figure 11: Transaction processing maturity

65% of organisations have consolidated to some extent

Less than 40% have a discrete and independent SSC organisation

Less than 20% use SSC for complex activities such as financial reporting and project accounting

It is interesting to note less than 30% of participants currently pursue more advanced sourcing strategies, such as outsourcing to a third-party provider, or retaining in-house but off-shoring. Despite the potential for further savings, it appears most organisations prefer in-house, on-shore alternatives.

The benefits of standardisation, consolidation and automation make the investment worthwhile. Irrespective of size and complexity top quartile participants operate at around half the cost of a typical finance function, while sustaining higher levels of insight, control and efficiency. All participants have initiatives underway to improve process standardisation, although the areas of finance addressed vary in each organisation.

IT in the finance function can be logically split into a number of areas – transactional, risk management, business intelligence and treasury systems. Our benchmark assessment shows substantial progress has been made in transaction processing in recent years through greater standardisation and the implementation of ERP solutions. Around 65% of participants have consolidated their transactional systems with some level of process standardisation. However, as Figure 12 highlights, there is clearly room for improvement as top quartile performers are able to achieve much faster cycle times.

Business intelligence systems have seen less improvement. Most participants are dissatisfied with the data delivery process. Multiple sources of data and excessive use of spreadsheets are often blamed for the lack of timely and consistent MI to support decision-making, though of course the ability to interpret and utilise the data appropriately is also critical.

‘I believe we pay too much for poor quality.’

CEO, consumer goods sector

Figure 12: Days to close and report financial results

Looking forward

As operating models and competitive challenges continue to evolve, the findings from the benchmark study highlight three key hurdles that will need to be overcome to enable companies to leverage the full value of their finance functions:

- Ensuring finance has the right skills and capabilities to support the business operating model and satisfy the needs of the organisation
- Ensuring the delivery of consistent, accurate, timely and relevant MI to support decision-making and risk management across the business
- Standardising and simplifying processes and supporting technology to curb costs and enhance efficiency.

The financial crisis and resulting downturn have given CFOs greater prominence and influence within many organisations and they are well positioned to tackle these challenges. Their success will be a crucial factor in enabling smart firms to stay ahead of the pack.

Benchmarking evaluation

As finance functions seek to respond to new business demands, our benchmark analysis can provide a clear assessment of strengths, weaknesses and areas for improvement, while providing a baseline from which to measure progress.

The analysis combines a qualitative assessment and comparative metrics across the competing demands of business insight, efficiency and compliance and control (see Figure 13). Business insight combines such evaluations as a comparison of time spent on analysis and data gathering and an assessment of management's reliance on the resulting forecasts. Efficiency includes a range of key determinants including the complexity of systems and time to close/report. Compliance and control examines such areas as cost, accountability and risk management.

The resulting analysis not only compares these ratings to other similar organisations, but also seeks to assess whether they are operating in equilibrium and are meeting the overall objectives of the business. For example, over-emphasising cost may inhibit the function's ability to provide insight and value.

How to participate

The benchmark analysis is one of the services offered to PricewaterhouseCoopers audit and non-audit clients. If you would like to complete a benchmark assessment or would like more information please contact Garrett Cronin, Consulting Partner, PricewaterhouseCoopers Ireland or visit pwc.com/ie

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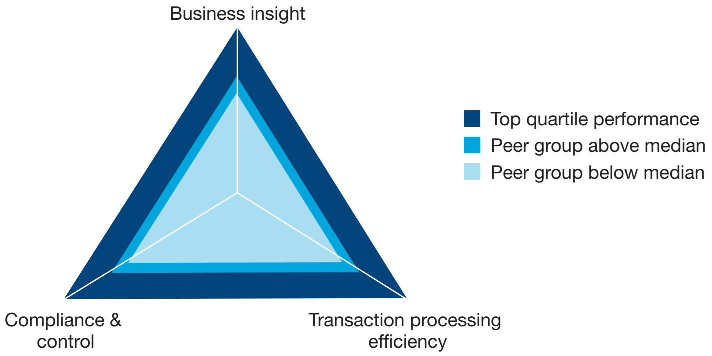
Figure 13: Competing demands



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