Strategies for Better Business Insight

A report prepared by CFO Research Services
in collaboration with IBM Software Group

CFO research services

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Contents

To: CFO Research Services
From: Senior finance executives
Date: Fall 2011
Re: Growth prospects

Dear CFO Research Services:

You may think from our recent response to your survey questionnaire, entitled "Strategies for Better Business Insight," that we see bright growth prospects ahead.

You'd be wrong.

The real picture is more complicated. Although a majority of us (52%) say that our companies' primary business objective over the next two years will be "identifying new growth opportunities" (and only 17% of us say that "controlling costs to maintain profitability" will be our main objective), this seemingly robust outlook isn't born from a sense of bright and abundant prospects. It is instead born of necessity.

Half of us—a full 50%—agree strongly that our companies "must increase revenue in order to maintain profitability; cost reduction will not be sufficient." Another 30% of us agree at least to some degree with that statement.

Furthermore, 83% of us think it'll be harder to maintain profitability over the next two years, compared with the last period, when the economy was growing.

We're pursuing growth because we have to—there's little left to cut, and we need to boost the top line in order to maintain profitability. The pressure is on to make the most of new paths to growth without surrendering profitability. It's already tough.

And it's about to get tougher.

Senior finance executives send a message

In the fall of 2011, CFO Research Services conducted a survey among senior finance executives at large and midsize companies across the United States. We wanted to understand how finance executives are thinking about the business environment in which they find themselves. What are the demands of this environment? How are companies preparing themselves to respond to those demands? And what role will finance, in particular, play in the effort to respond?

If senior finance executives could have gotten together to write us a memorandum about the pressures they face, the results of our survey strongly suggest they would have written one like the one opposite.

But this "memo" from finance executives is only the beginning of the story.

This story is about how finance executives and their companies are attacking the problem of growth in an exceptionally volatile and risky period in our shared economic history. The good news is that the global economy is showing signs of a sustained, if not entirely robust, recovery. But there are few sure routes to growth in this environment, and the finance executives who participated in our survey recognize that simply managing for growth won't be enough. Sustained and profitable growth is the order of the day.

Finance executives, for their part, will contribute to the pursuit of sustained, profitable growth by improving the sourcing and analysis of performance information—and by ensuring that decision makers are able to apply that analysis to their work while it can still make a difference. In this report, we'll explore finance executives' information and management strategies for gaining insight into their businesses and communicating that insight to those who need it most.

Sustained and profitable growth is the order of the day.

About this report

In September 2011, CFO Research Services conducted a survey among senior finance executives at U.S. companies with annual revenues of $100 million or more to examine their views on managing performance in the current business environment.

We gathered a total of 184 complete survey responses. Respondents work for companies in a broad range of company segments, as follows:

Annual revenue (in US$)	
$100 million to $500 million	33%
$500 million to $1 billion	15%
$1 billion to $5 billion	30%
$5 billion+	22%

Titles	
Chief financial officer	32%
Director of finance	16%
VP of finance	16%
Controller	14%
Finance manager	8%
EVP or SVP of finance	6%
Treasurer	2%
CEO, president, or managing director	2%
Other C-suite executive with finance responsibilities	2%
Other	4%

Respondents work for companies in nearly every industry. The financial services, real estate, insurance, and manufacturing industries are particularly well represented.

Note: Percentages may not total 100%, due to rounding.

Challenging business conditions raise the stakes on performance management

Mounting pressure to achieve sustained, profitable growth is reflected in companies' performance-management priorities. Finance executives frequently report, for example, that their companies assign a high degree of priority to improving profitability analysis. Sixty percent of respondents say that improving their companies' ability to analyze and understand profitability will be a high priority over the next two years—and more than half of all respondents (53%) say that expanding the scope of profitability analysis will be a high priority. Improving performance reporting to decision makers (60%) and improving forecasting (58%) are also likely to be high priorities. (See Figure 1.)

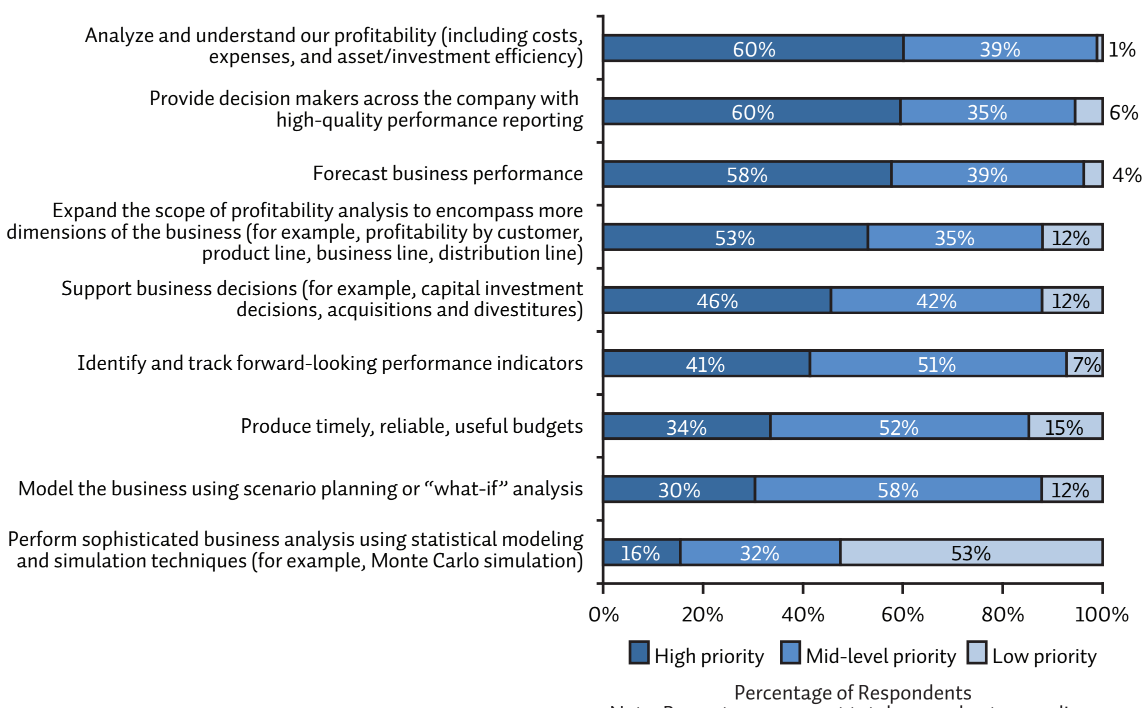
But even as finance executives confirm that they want to understand profitability better, report to decision makers more effectively, and produce more-useful and more-timely forecasts, they acknowledge that core performance-management activities are likely to become more challenging to perform well over the next two years than they have been in the past.

Many of these difficulties are linked, of course, to persistent uncertainty and volatility, exacerbated by a combination of deep cuts in pursuit of greater efficiency and increasingly complex global operating profiles. Finance executives most often report that performance-management activities tied closely to predicting future outcomes and responding to changing circumstances will be more challenging over the next two years. Sixty-two percent of respondents, for example, say that identifying and mitigating risks to performance will be at least somewhat more challenging over the next two years. The stakes for identifying and countering threats are high—the tolerance for error narrowed over the

Figure 1: Finance executives prioritize improving their companies' ability to analyze and understand profitability.

Over the next two years, what degree of priority will your company assign to the following improvement initiatives?

Improving our ability to….



Note: Percentages may not total 100%, due to rounding.

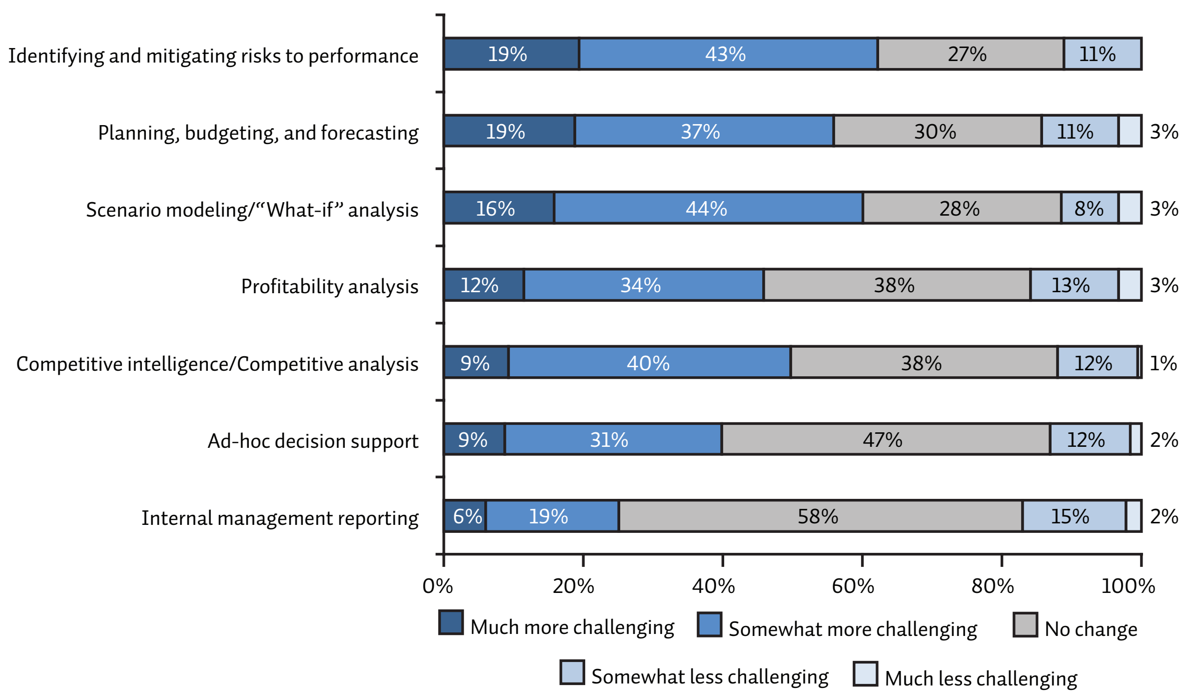
course of the downturn as companies made deep cuts to maintain their profitability. Although many companies have moved to improve their risk-management capabilities during the economic crisis, these results show that companies will struggle to manage threats to performance for some time to come.

Another activity tied to predicting future outcomes and managing uncertainty—"what-if" analysis—is also likely to be difficult in the years ahead. Sixty percent of respondents say that what-if analysis will be more challenging over the next two years. Meanwhile, more than half of all respondents (56%) say that planning, budgeting, and forecasting—the core finance activity that expresses the very essence of anticipating and responding to change—will be more challenging. (See Figure 2.)

Analyzing and understanding profitability will be a high priority.

Figure 2: Core performance-management activities are expected to be more difficult over the next two years than they were during the last period of economic expansion.

In your opinion, will it be more or less challenging to perform the following performance-management activities effectively over the next two years, compared to the last period of economic expansion?



Percentage of Respondents
Note: Percentages may not total 100%, due to rounding.

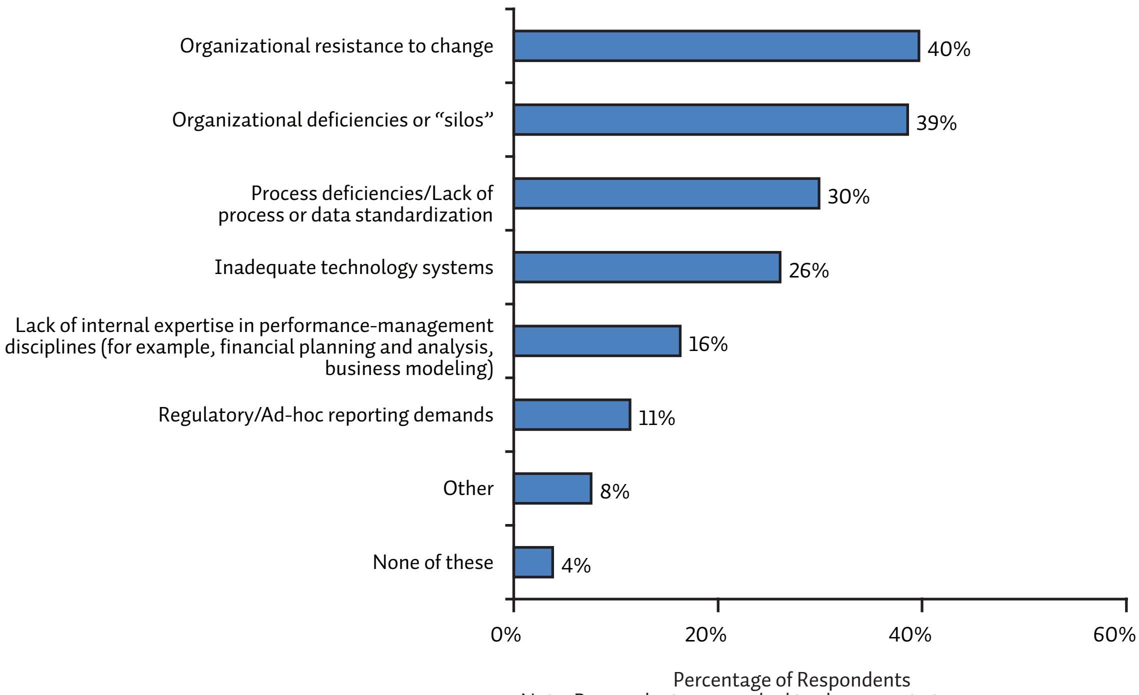
Finance executives see promise in better organizational alignment

The "people, processes, and systems" formulation is a classic paradigm that can be used to describe any number of systems-implementation and change-management efforts. But if gaining organizational support and eliciting a commitment to change are the first steps in that improvement paradigm, the results of this study show that many companies have a lot of ground to cover. Organizational difficulties pose the greatest barriers to improving performance management, according to the finance executives we surveyed. Respondents most often cite organizational resistance to change (40%) and organizational deficiencies or "silos" (39%) among the greatest barriers to improvement at their companies. Process deficiencies/lack of process or data standardization (30%) and inadequate technology systems (26%) follow. (See Figure 3.)

> If gaining organizational support and commitment to change are first steps toward improvement, many companies have a lot of ground to cover.

Figure 3: Organizational difficulties pose the greatest barriers to improving performance management.

Aside from resource scarcity, which of the following problems pose the greatest barriers to improving your company's ability to manage its performance?



Note: Respondents were asked to choose up to two responses. Percentages will not total 100%, due to multiple responses.

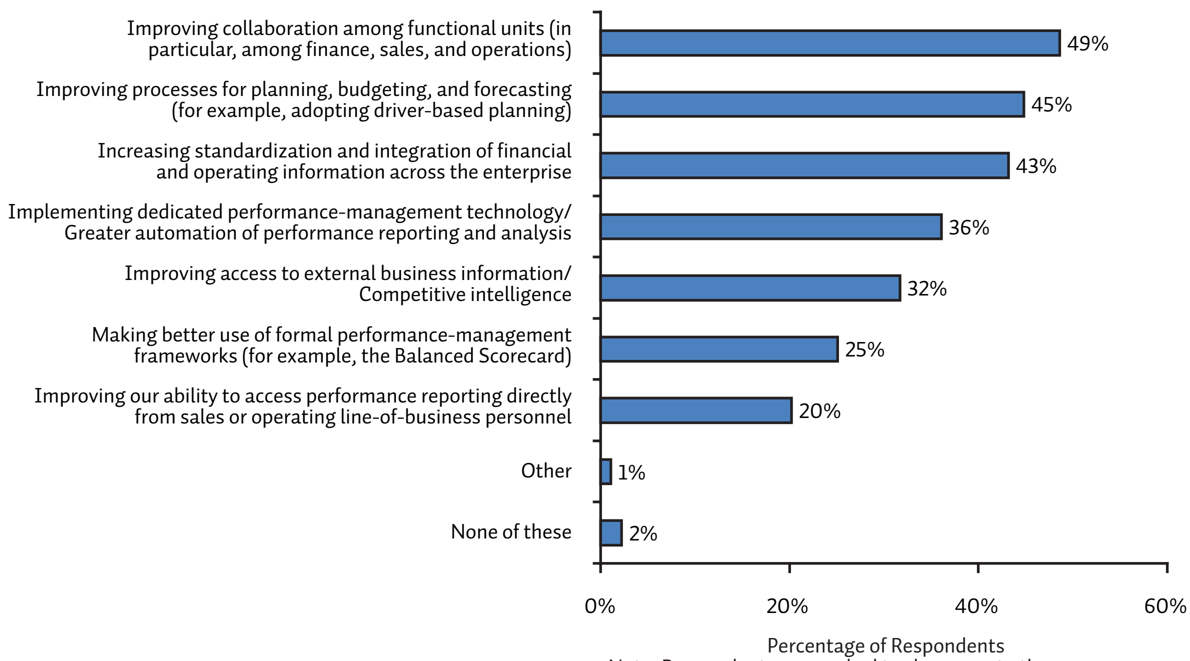
It's not very surprising, then, that finance executives say that better organizational alignment (including improved collaboration and more tightly integrated information), together with improved processes for planning, budgeting, and forecasting, would contribute most to companies' ability to meet their performance-management priorities.

Respondents most frequently cite improving collaboration among functional units as one of the changes that would contribute most to their ability to realize their performance-management priorities (49%). Forty-five percent of respondents say that improving processes for planning, budgeting, and forecasting would be among the changes that would contribute most to their ability to realize these priorities, and nearly as many (43%) say that increasing standardization and integration of financial and operating information across the enterprise would make a great contribution to their ability to meet those priorities. (See Figure 4.)

Improving collaboration among functional units is one of the changes that would contribute most to realizing performance-management priorities.

Figure 4: Senior finance executives see significant value in improving collaboration among functional units.

In your opinion, which of the following changes would contribute most to your company's ability to realize its performance-management priorities over the next two years?



Note: Respondents were asked to choose up to three responses. Percentages will not total 100%, due to multiple responses.

A wider scope of information and analysis may improve profitability management

If greater organizational alignment is one prerequisite for better performance management, what else would a closely aligned organization—an organization equipped with a meaningful capacity for concerted effort—need in its pursuit of sustained and profitable growth? A better understanding of how, where, and when to apply that effort.

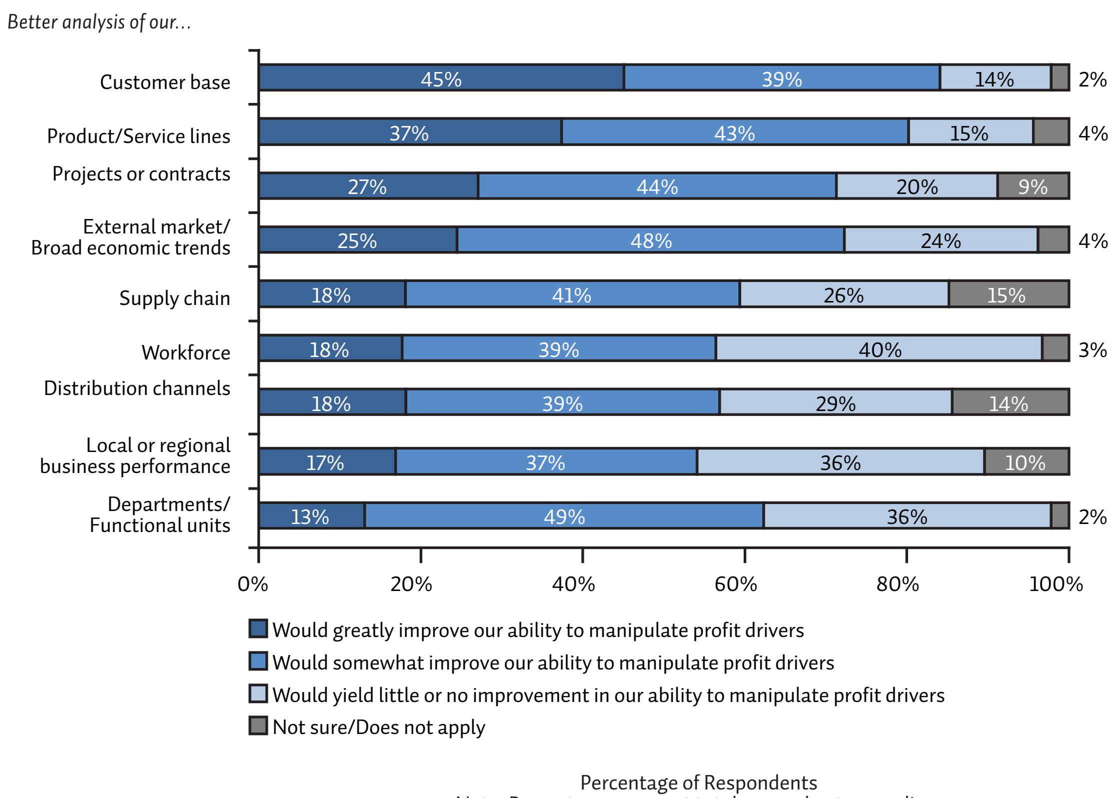
Finance executives responding to our survey recognize that improving the analysis of most major business dimensions would improve companies' ability to effectively manipulate profit drivers (including price, variable and fixed costs, and sales volume). Better analysis of customers and better analysis of product or service lines are particularly likely to contribute substantially to the ability to effectively manipulate profit drivers.

Forty-five percent of respondents say that better analysis of their customers would greatly improve their companies' ability to manipulate profit drivers; 37% of respondents say that better analysis of their product or service lines would yield great improvement. (See Figure 5.)

Ultimately, companies are working to understand where they're making money and where they aren't—which in turn requires a deeper comprehension of the full range of their costs (including the cost of sales, production, delivery, and service) as well as the spending behaviors and needs of their customers. Within a given customer base, for example, growth opportunity—and competitive vulnerability—often reside with customers that can afford to pay well but are underserved. Certain product lines may yield impressive gross margins but disappoint on closer inspection, due to an outsize cost of service over time. Better analysis of customers can reveal these types of opportunities, vulnerabilities, and problems.

Figure 5: Finance executives' ability to manipulate profit drivers would benefit most from better analysis of customer base.

To what extent would better analysis of each of the following dimensions of your business improve your ability to effectively manipulate profit drivers (e.g., price, variable and fixed costs, and sales volume)?



Note: Percentages may not total 100%, due to rounding.

In addition to that improved analysis, however, the results of our survey suggest that companies need access to more-detailed, more-abundant information in order to manage their profitability better.

For example, when presented with two broad approaches to sourcing and analyzing performance information—expanding the scope of information to create a more robust basis for decision making or narrowing the scope of information in order to speed analysis and improve responsiveness—finance executives choose expansion: a majority of respondents (55%) say their companies are most likely to expand the scope of information in order to manage profitability. Only 31% of respondents say they plan to narrow the scope of information. (See Figure 6.)

Growth opportunity and competitive vulnerability often reside with customers that can afford to pay well but are underserved.

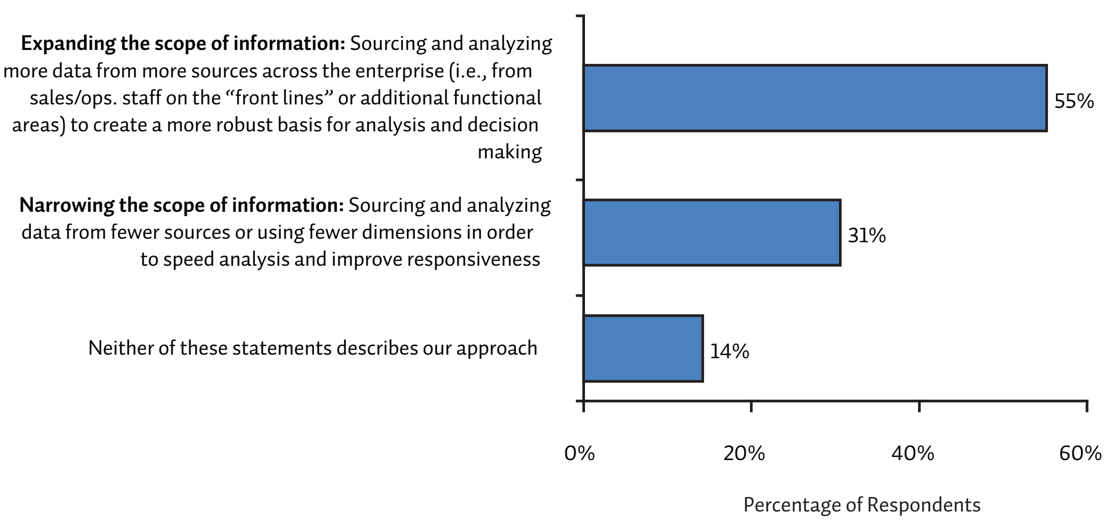
Process discipline and sophisticated technology help companies make use of large volumes of data

Although finance executives as a group—when forced to choose—are more interested in information expansion over information streamlining, these results by no means represent a rejection of speedy analysis or quicker action. Finance executives and their companies plan to deploy additional strategies aimed at managing their information and gaining control of growing pools of performance data.

One strategy for gaining control over large amounts of data involves process discipline: setting information priorities and applying monitoring and analysis efforts accordingly. Broadly speaking, the most relevant and the most volatile financial and operating metrics should be higher priorities—and should benefit from greater attention as a result.

Figure 6: Companies are most likely to expand the scope of performance information in order to better manage profitability.

In your opinion, which of the following approaches to sourcing and analyzing performance information is your company most likely to take to improve its ability to manage its profitability?

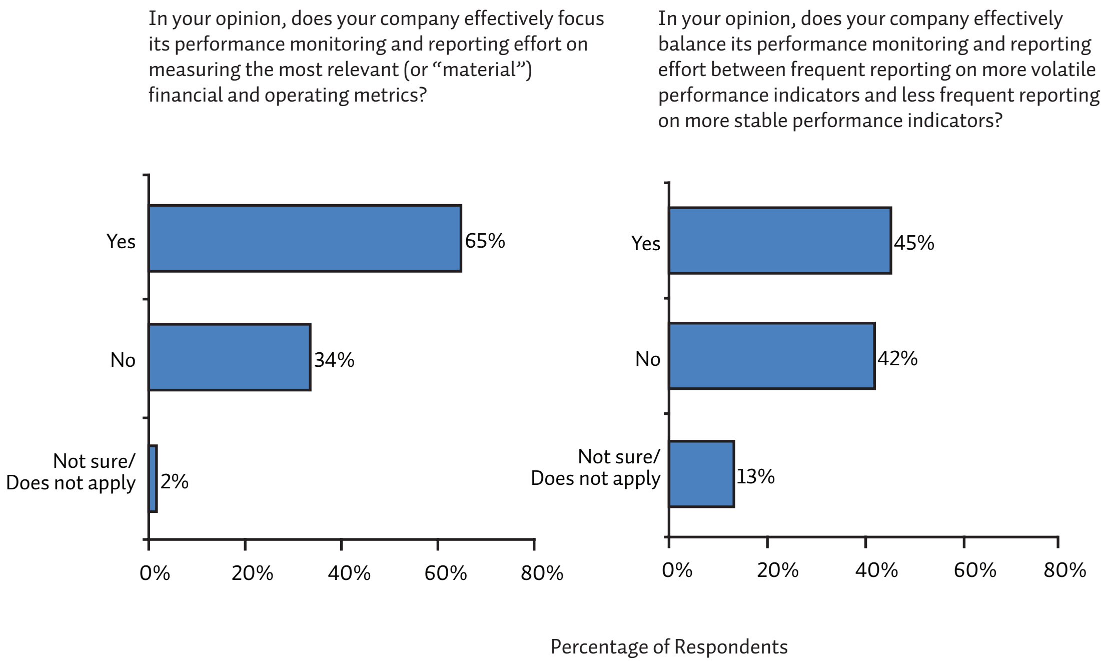


How successfully are companies setting those priorities and focusing their information efforts? The results of our survey are mixed. In general, finance executives are more confident in their ability to concentrate their efforts on the most relevant metrics than they are in their ability to balance their reporting efforts effectively between more-volatile and more-stable performance indicators. Nearly two-thirds of all respondents (65%) confirm that their companies effectively focus on measuring the most relevant or "material" financial and operating metrics. But when it comes to dividing their reporting effort between more-volatile and more-stable metrics, those who confirm they strike this balance well slightly outnumber those who say they don't (45% vs. 42%). (See Figure 7.)

Another strategy for making the most of vast stores of information involves a combination of technology systems and analytical skill. Robust technology systems can certainly support companies' efforts to access the most relevant data and closely monitor the most volatile data. Indeed, technological progress—exponential leaps in storage capacity and processing power—feeds the aspiration for more-robust information even as it satisfies that aspiration. Over the course of the IT revolution, technology has made it possible to source more data more reliably, and to analyze and report information more quickly. Technological progress will no doubt continue to press out the boundaries of what's possible.

At the same time, the results of our survey show that some companies are making better use of technology than others: we found a correlation between the adoption of highly sophisticated, "best-of-breed" technology systems for reporting, planning, and analysis and the ability to access crucial information.

Figure 7: Finance executives are generally confident in their ability to prioritize financial and operating metrics according to their relevance. They are somewhat less confident in their ability to balance their reporting effort based on the relative volatility of performance indicators.



Sophisticated technology systems are linked to an improved ability to manage performance

Users of dedicated, best-of-breed technology systems for reporting, planning, and analysis are much more likely than their peers to say their decision makers have access to useful leading performance indicators. Nearly two-thirds (64%) of respondents using best-of-breed technology systems for performance management confirm that their decision makers consistently have access to useful leading performance indicators, compared to 43% of respondents using a financial application module of an ERP system, 38% of respondents deploying point solutions, and only 29% of respondents primarily using spreadsheets and manual processes. (See Table 1.)

A similar trend emerges between users of best-of-breed technology systems and those who confirm that their decision makers have access to useful external information. (See Table 2.)

Furthermore, when queried explicitly on the contribution their technology systems have made to their companies' ability to manage profitability effectively, users of dedicated applications for performance management are much more likely than their peers to confirm that their technology systems have made a substantial, positive contribution. (See Table 3.)

Table 1. Best-of-breed application users more often say they have access to useful leading indicators of performance.

Type of system	Percentage confirming consistent access to useful leading indicators	Difference compared to dedicated ("best-of-breed") application (in % pts)
Dedicated, best-of-breed application for performance management (n=36)	64%	-0-
Financial application module of an ERP system (n=63)	43%	-21% points
Point solutions with gaps (n=32)	38%	-26% points
Primarily spreadsheets and manual processes (n=46)	29%	-35% points

Table 2. Best-of-breed application users more frequently confirm they have consistent access to useful external information (such as benchmarking data and competitive intelligence).

Type of system	Percentage confirming consistent access to useful external information	Difference compared to dedicated ("best-of-breed") application (in % pts)
Dedicated, best-of-breed application for performance management (n=36)	67%	-0-
Financial application module of an ERP system (n=63)	62%	-5% points
Point solutions with gaps (n=32)	41%	-26% points
Primarily spreadsheets and manual processes (n=46)	49%	-18% points

Table 3. Best-of-breed application users are more likely than their peers to confirm that their technology systems have made a substantial contribution to their ability to manage profitability.

Type of system	Percentage confirming substantial contribution of technology systems to ability to manage profitability	Difference compared to dedicated ("best-of-breed") application (in % pts)
Dedicated, best-of-breed application for performance management (n=36)	33%	-0-
Financial application module of an ERP system (n=63)	19%	-14% points
Point solutions with gaps (n=32)	13%	-20% points
Primarily spreadsheets and manual processes (n=46)	4%	-29% points

The finance executives who participated in this study confirm that the days of improving profitability through cost reduction are over: finding new growth opportunities is the current imperative. But returning to growth, by itself, isn't enough. Companies are pursuing sustained, profitable growth—in a volatile, uncertain, and competitive business environment that threatens margins as well as growth trajectories.

Finance executives recognize that better organizational alignment and a wider scope of information and analysis can improve companies' ability to take full and profitable advantage of the opportunities within their reach. But even as they aspire to expand the scope of information—to source information in real time directly from the shop-room floor and the front lines of sales—finance executives suggest that their performance in applying process discipline to the task of managing large volumes of information is mixed.

One of the most important avenues to better information management and more-robust, useful analysis is technology improvement. The results of our survey show that finance executives recognize the contribution that dedicated, best-of-breed systems for performance management make to effective profitability management—especially when compared with spreadsheets and manual processes. Survey results also show a relationship between adoption of best-of-breed performance-management systems and access to both useful leading indicators of performance and external information (including benchmarks and competitive intelligence).

The business environment is tough, and the finance executives who participated in this study see plenty of challenges ahead. But this research shows that finance executives are ready to tackle the organizational, process, and technology changes that will help their companies write their story of success in this new era of uncertainty.

Broader collaboration, deeper analysis, better insight

As the volatility and pace of business increase, finance executives are under increasing pressure to deliver stronger business insight to help their companies grow profits and revenue and improve return on invested capital.

Yet the majority of finance executives believe that developing such insight, through identifying and mitigating risk, planning, budgeting and forecasting, as well as scenario modeling and what-if analysis, will all be more challenging over the next two years (See Figure 2, page 5).

The CFO report cited the following as the three strongest contributors to realizing key performance management priorities: 1) improving collaboration among functional units; 2) enhancing the core planning, budgeting and forecasting process; and 3) increasing integration of financial and operational information across the enterprise (See Figure 4, page 7).

This research shows a connection between adopting dedicated performance management applications and the ability to access leading performance indicators. Respondents who use dedicated applications for performance management are also more likely to say that their technology systems have made a "substantial contribution" to their ability to manage profitability, compared to their peers who use spreadsheets and manual methods, patchworks of point solutions, or even ERP modules (See Table 3, page 11). At IBM®, we refer to these dedicated performance management applications and related practices as "business analytics."

Where should companies seeking to deliver stronger insights through business analytics start? We recommend five practical steps.

1) Automate performance monitoring
Effective measurement and monitoring ensures that "what gets measured gets managed." An effective monitoring solution should:

- Automate the production of financial and operational metrics to reduce errors, reduce staff effort, and improve data governance
- Create lead time for the organization by incorporating leading and predictive indicators into the measurement system instead of over-relying on lagging indicators
- Consider materiality and volatility in those metrics that provide insight for decision making
- Match the refresh rate of metrics to a frequency that reflects market volatility in order to sharpen focus and reduce effort
- Connect metrics to corporate objectives

2) Deliver fast, reliable reporting
Virtually every organization creates reports. Unfortunately, the quality, timeliness and usefulness of those reports vary dramatically. Desirable reports are those that:

- Provide the right level of financial and operational detail
- Provide timely, relevant information in a variety of formats, including scorecards and dashboards, and in a variety of mediums, from web to electronic publishing to mobile devices
- Connect to all performance views–historical, latest forecast-projected plan, and current goals
- Coordinate at all levels, from summary to detail
- Adapt readily to changing organizational goals and business conditions

3) Make planning a part of your culture
Help users align individual or departmental goals with the broader corporate strategy. Best-practice planning can:

- Connect financial and operational drivers
- Enable rolling horizons in proportion to the lead time needed to respond to changing conditions
- Deliver plans at the appropriate frequency, matched to volatility and materiality
- Enable range forecasting and scenario planning to account for risk and uncertainty
- Enable collaborative planning through automated workflow and process management
- Feed new information back into ongoing measuring and reporting systems

4) Analyze and understand the business
Gain a better understanding of which drivers impact the business, and which customers and products are the most profitable. Useful analysis capabilities enable you to:

- Model the business and define multiple dimensional views, such as product, customer, channel, region, sales rep, or cost center
- Model financial and operational results–cash flow, customer profitability, product profitability and revenue performance–to quantitatively measure inputs and outputs
- Perform what-if analysis to examine options when business conditions change

Sponsor's Perspective

5) Broaden the scope of risk management
Manage risk across the entire organization, from the operational risk of breakdowns in the supply chain, to financial risks affecting income, balance sheet and cash flow. An effective risk management approach helps you:

- Understand where risk exists, and establish risk indicators linked to KPIs and avoidance or mitigation strategies
- Model risk with analytics and link risk metrics and probabilities to actual plans and forecasts
- Deploy open data and systems to expose information to more people and reveal hidden, previously undetected dangers
- Automate, enhance or extend business controls to monitor and prevent risk

The global economic crisis has put CFOs in the spotlight as never before. Fortunately, CFOs and their finance organizations now have better tools than ever before and a broader repertoire of proven best-practices to help them meet the challenge of the current economy. The broad portfolio of IBM Cognos® and IBM SPSS® products includes solutions for:

- Scorecarding and strategy management
- Planning, budgeting and forecasting
- Financial analytics to improve understanding of profit drivers
- Financial consolidation and corporate reporting
- Analysis of transaction information across financial and operational systems
- Predictive analytics to gain new insights into profit and growth opportunities

With so many sophisticated solutions available, virtually any finance organization can find a logical, cost-effective starting point for the journey to greater process efficiency and greater business insight. And at IBM, we're ready to help.

About IBM Business Analytics
IBM Business Analytics software delivers actionable insights that decision-makers need to achieve better business performance. IBM offers a comprehensive, unified portfolio of business intelligence, predictive and advanced analytics, financial performance and strategy management, governance, risk and compliance and analytic applications.

With IBM software, companies can spot trends, patterns and anomalies, compare "what-if" scenarios, predict potential threats and opportunities, identify and manage key business risks and plan, budget and forecast resources. With these deep analytic capabilities our customers around the world can better understand, anticipate and shape business outcomes.

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