CAN FINANCE BE BOTH EFFECTIVE & EFFICIENT?

Most Finance organizations have become focused on driving down costs, achieving a cost/revenue ratio of 1% or less. If your organization is one who has efficiently achieved under 1%, can you also say that you are effectively aligned with your corporate strategy and objectives?

Practical solutions that work.
Balancing Efficiency & Effectiveness in Finance

Why has Finance only focused on efficiency?

Finance, like most support functions, has been pressured to focus inward to reduce their costs. Most organizations have become myopically focused on driving down finance costs as a percentage of revenue. Through this focus, many finance organizations have achieved a cost/revenue ratio of 1% or less. Costs have been reduced over 40% through automation, new operating models, leaner processes and even elimination of some services. Why has cost take-out been the primary driver for finance functions over the last 20 years? We believe it is because cost KPI’s are relatively easy to calculate and benchmark data has become ubiquitous as well as the demand for increased corporate profits. With cost data seemingly everywhere, it is easy for managers to focus on the efficiency factor. Additionally, workable frameworks have not been developed that combine the viewpoint of achieving effectiveness with efficiency.

If you are one of the many who have achieved 1% of revenue or less and are now deemed efficient, can you also say that you are effectively aligned with your corporate strategy and objectives? The answer is likely no, because there has been little or no development of formalized ways to measure the degree of effectiveness of finance organizations.

You must find a way to balance efficiency and effectiveness to be a valued advisor to the business. Effectiveness is the foundation of success—efficiency is a parameter for survival. Can finance be both effective and efficient? This white paper will show you that it is possible as long as you take a structured approach to tie the strategic objectives of the organization to success measures and then on to functions that finance performs. If you can directly link strategic objectives to success measures in finance, you can focus your efforts on what is important which promotes both the efficiency and effectiveness of finance. It will also enable the CFO to have an informed conversation with the business leaders when evaluating the trade-offs of further efficiency programs or investments in programs for increased effectiveness, which will deliver higher returns.

What are the Current Trends & Drivers?

For the past 20 years, most improvement efforts in finance have been focused on increasing efficiency through labor arbitrage (outsourcing), reduction of service levels, and further automation of routine tasks.

The top trends for finance today continue to be focused on achieving efficiency and not on increasing and measuring the effectiveness of finance to the rest of the organization. The emphasis on achieving efficiency will continue to erode the value of the finance department to the rest of the organization.

Solely focusing on cost metrics is a self-perpetuating process where the finance organization will be viewed as a cost center versus a business partner.

To drive this ongoing improvement, we recommend the Finance R&D approach outlined in our whitepaper, “How to Make Your Next Transformation Your Last”.
Trends in finance today, such as finance transformation, lean processes and robotics, are all singularly focused on driving efficiency and lowering the cost of finance. However, these trends fall short in increasing the value of the finance function to their business partners. There is little focus on how to provide the right services to the right customers at the right time. In order to strive towards world class performance, a finance organization must establish a balanced approach of efficiency and effectiveness. CFO’s should view any initiative whether it be finance transformation, lean processes or robotics as an opportunity to increase the value of finance to the business.

Finance organizations embrace these trends and undertake initiatives due to a variety of reasons, but they often fail to clearly identify the multifaceted objectives they are trying to achieve because they are slavishly pursuing the percentage of revenue cost target versus linking to the objectives of their business partners and corporate strategy. Implementation of these trends can also increase effectiveness of the organization, when combined with a measured view of efficiency. A successful program would link Finance’s objectives and measures to the key requirements of the broader business and the customers of finance. A structured approach for finance would involve implementing cost reduction programs in parallel to also

**FIGURE 1:**
Creating a Balance of Efficiency & Effectiveness

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Customer
Shareholders
Regulators

Demands

Valued Products/Services
Increased Share Value
Compliance

Drives

Business Strategy

Shapes

Business Operating Model
Finance Operating Model

Generates

Joint Goals & Measures

Determines

Business & Finance Activities & Programs

Creates a balance of

EFFICIENCY
EFFECTIVENESS
developing a better view of the customer of finance. To align to the transformation efforts underway in many companies, CFO’s will need to adopt new operating models more closely tied to the customer experience objectives of these efforts. McKinsey & Company had this observation when delivering transformation on an enterprise level but it applies to the finance organization as well. “To build value and provide compelling and effective customer experiences at a lower cost, organizations need to commit to a next-generation operating model. This operating model is a new way of running the organization that combines digital technologies and operations capabilities in an integrated, well-sequenced way to achieve step-change improvements in revenue, customer experience, and cost”.

For finance however, linking their service delivery model to the desired business outcomes and customer experience is not a single step process. The desired business outcomes will give rise to performance metrics that are supported by the activities that make up the experience of customer of finance. Finance would then need to develop related metrics for finance that both measure the customer experience and are also drivers or inputs into the measures of business outcome. When viewing finance through these customer experience and success measures the focus shifts from what it has been, the singular objective of cost takeout from finance.

What Should Finance Focus on to Increase Effectiveness?

The extensive range of services that finance must offer to meet the diverse requirements of internal and external customers make it difficult to determine what to focus on and prioritize. Finance has obligations to meet legal, tax and compliance mandates, provide transactional and technical support to the business and deliver financial and management reporting. To effectively meet those diverse needs, Finance must understand the requirements of each customer and the drivers of the business in order to provide services which promote the effective and efficient achievement of their objectives. As with companies that are able to transform an industry sector, the first step in developing the next-generation operating model is to map key customer journeys. By identifying a set of key customer journeys for the customers of finance, we can then reimagine the customer experience. By taking this approach, the finance function can avoid the trap of trying to improve existing processes instead of dramatically changing the way the customer experience is delivered. As a result, this would inform the operating model and the related effectiveness measures that finance can link either to business outcomes or the customer experience or better yet both. The direct linkage of the success measures for finance will result in the improved focus of the finance function on areas that are key drivers for the success of the business. This focus will help finance to deliver the right things in an efficient manner, or in other words this behavior will result in finance improving effectiveness.

As finance organizations gain better insights into what the customer values they can shift their focus from a pure annual cost take-out approach to a multi-year portfolio return approach that views investments in finance capabilities as a direct return on the business performance. These investments can then be viewed in ROI terms as it relates to the achievement of broader corporate goals and the experience of the customer of finance. Effectiveness of a finance function is measured by achievement of goals which have been aligned with their business partners.

How do you Start?

First you need to define Effectiveness. Effectiveness is the degree to which something is successful in producing a desired result; success. For simplicity, we define effectiveness as doing the right things in order to produce the expected outcome. In order to deliver effectiveness, you must first start by identifying the right things. This should be done both in a way that aligns to the customer journey, the customer of finance, and the related corporate strategy. By viewing the delivery of the services of finance from the customer journey perspective, it will both improve the focus on what is important to the customer while also removing the constraints of the way finance currently operates. What we mean by this is that if you reimagine the way in which finance delivers services to the customer from the customer perspective, you are no longer constrained to trying to iteratively improve
the current finance operating model but you can then
dramatically change that operating model while focusing
the outcome on the key mission the customer objective.

The customer journey has been shaping how companies
organize their strategy and the related business models
but it can also be used to tie directly through to the
finance operating model. If we are able to tie finance
operations measures directly to their related business
success measures, then we can understand how truly
effective the finance function is.

By aligning finance operations to the business objectives
more directly, you will be able to identify areas that
directly affect the desired results of the business. By
definition, this aligns to the definition of effectiveness
from Peter Drucker “effectiveness is doing the right things.
Now that the organization can understand what they
should be doing, what the right things are, they can then
start to optimize around those focus areas.

What are Some Examples of Effective Measures?

Measures of effectiveness can be leading or lagging.
Lagging indicators confirm that your performance has
been effective or not. They measure the result of past
actions. Leading indicators predict the effectiveness
of your performance. They measure actions which will
affect future organizational effectiveness. You will want to
have a mix of these indicators but your focus should be
on leading indicators which measure results and actions
with an emphasis on results. The performance indicators
should strive to measure the effectiveness of actions
which informs decision making, improves your customer’s
journey, reduces cost and drives profitable contributions
to the organization. You need to align these measures with
your business partners and ensure that there is data readily
available to support the effectiveness measures adopted.

**FIGURE 2:**
Effectiveness Metrics
Translating Business Objectives into Actionable Finance Measures

<table>
<thead>
<tr>
<th>Business Objective</th>
<th>Indicator</th>
<th>Measure of Effectiveness for Finance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increase Revenue and Reduce Cost</td>
<td>Increase in Profitable Growth</td>
<td># of business decisions initiated/supported that increased margin, % margin amount increased</td>
</tr>
<tr>
<td>Increase Customer Base</td>
<td>New profitable business opportunities identified</td>
<td># of profitable opportunities identified</td>
</tr>
<tr>
<td>Identify and enter new markets/geographies</td>
<td># of new markets/geographies</td>
<td># of new markets identified and/or supported with empirical data</td>
</tr>
<tr>
<td>Increase Internal Customer Satisfaction</td>
<td>Net Promoter Score</td>
<td>Exceeding a benchmark established by your business partners and/or external benchmarks</td>
</tr>
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Types of Effective Behaviors

**Decision Support**
- Identifies business opportunities to increase margins.
- Supports business decisions with empirical information.

**Corporate Services**
- Produces information that drives decisions to review and reduce facility, travel and other administrative costs.

**Compliance Services**
- Drives regulatory agendas to benefit business.

**Revenue Accounting**
- Produces trend reports to identify seasonality and future buying habits.

**Accounts Payable Services**
- Identifies top vendor spend and engages with Procurement to negotiate OEM’s thereby reducing cost.
To Balance Efficiency & Effectiveness

You must balance efficiency and effectiveness for finance to become a valued advisor to the business. You need to avoid the traditional finance focus on saving costs and instead look at the effectiveness of your organization through the eyes of your customers.

The journey to become an effective finance function will require a multi-dimensional approach and traditionally different mindset. All aspects of the finance operating model, processes, people and technology will need to be examined and aligned to the customer journey, the corporate strategy and the business objectives.

CFOs must examine their current finance structure and align their operating model strategy to their customer and ensure they are meeting their business strategies and objectives. They must stand back and look at their services through their customer’s eyes in order to evaluate the effectiveness of the services. Identifying business opportunities and delivering meaningful information to drive decision making should be your overarching goals.

We believe the Fundamentals to the Balancing of Effectiveness and Efficiency are:

• Identification of your customers
• Agreement on information or services required by your customers
• Creation of finance objectives which support customer and business objectives
• Alignment of your operating model to customer demands and business strategy
• Development of lean processes which support your customers and the business strategy
• Enablement of technology to support production of actionable information

• Staffing and training your employees to recognize and deliver value
• Establishment of finance Effectiveness objectives and measures

To build an effective and efficient organization you need to ensure you are providing value-added information, you are meeting customer demands, compliance requirements, and you can measure your effective performance on an ongoing basis. This will be a journey with continuous improvement as your customer demands and business strategy are ever evolving.

“Efficiency is doing things right; effectiveness is doing the right things.” —Peter Drucker

Clarendon Partners combines extensive industry knowledge with business skills that allow us to deliver pragmatic advice and guidance to help our clients improve performance, effectively manage risk, and gain insights from data in order to achieve their business objectives. Rather than following a formulaic methodology, we tailor our approach to each engagement to improve the outcomes for our clients.