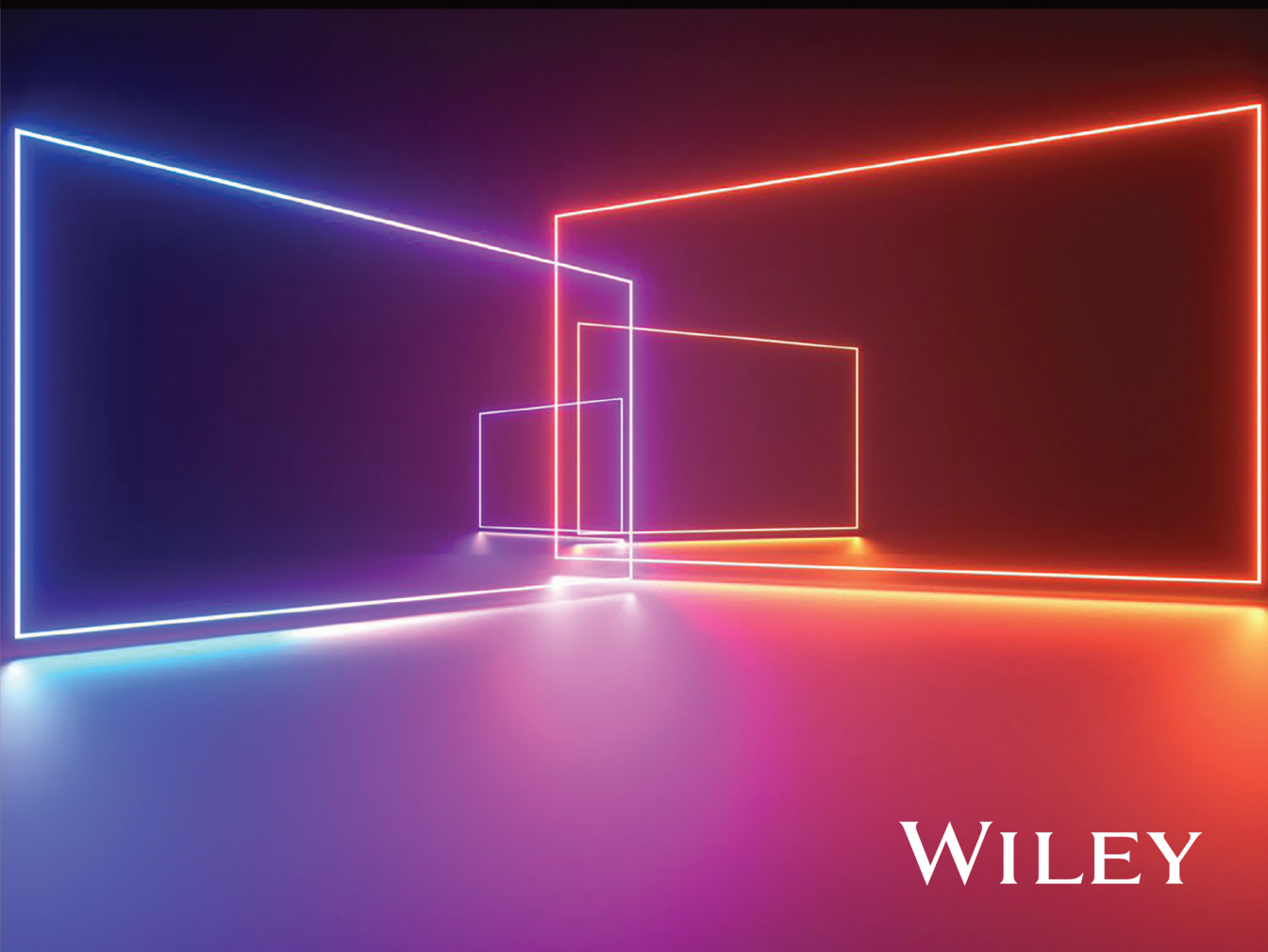


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# FINANCIAL MANAGEMENT

Partner in Driving Performance and Value

**JACK ALEXANDER**



**WILEY**



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# **FINANCIAL MANAGEMENT**



# FINANCIAL MANAGEMENT

PARTNER IN DRIVING  
PERFORMANCE AND VALUE

Jack Alexander

WILEY

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To my family:

My wife Suzanne, for five decades of love, support, and friendship.

My parents Marian and Jack, who are at peace with the Father.

My sons Rob and Tom, and their wives Courtney and Felicity.

My sisters Karen and Carol, and their families.

And especially to my granddaughters Emmy and Lienna, who bring  
indescribable joy and happiness to our lives!



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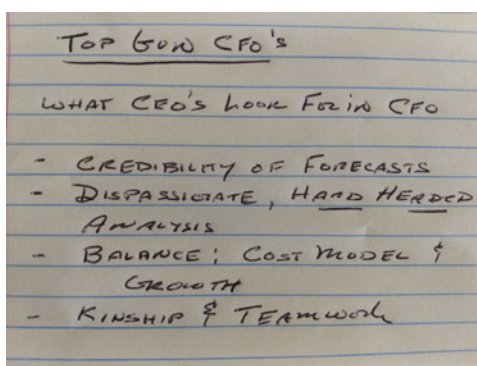
# Preface

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## WHY THIS BOOK?

In the late 1970s, as I was starting my career, I came across an article that identified the traits a chief executive officer was looking for in a chief financial officer (CFO). Since I had already set my sights on becoming a CFO, I jotted down the key takeaways from the article, something that I developed a habit of doing over my career and continue to this time. Unfortunately, I did not note the article, publication, or CEO to give them credit here or to recognize the soundness of the points articulated in the article. Figure P.1 is a copy of my notes that I have retained to this day:

FIGURE P.1 **Top Gun CFOs.**



My initial reaction to the article was a realization that the CEOs did not include many of the traditional functions in accounting and finance, including control and external reporting (my role in public accounting at the time of the

article), transaction processing, tax, treasury, and many others. Over time I recognized that CEOs and boards take these functions for granted. . . unless there are weaknesses or issues! Finance executives must execute well on the blocking and tackling *and* provide the service and advice appreciated by CEOs.

Each of the recommendations has proven to be true in my experience and form the foundation of being a “Partner in Driving Performance and Value.” Of course, this assumes that financial controls and reporting are also well executed. CFOs and finance teams must be able to develop, evaluate, and assist in achieving planned and forecast results. The succinct phrase “dispassionate, hard-headed analysis” made a deep and lasting impression. Financial leadership must be impartial and objective. Finance teams must be prepared to identify and expose both problems and opportunities, often in a hard-headed way. CFOs and their teams must strike a balance between focusing on the cost model and directly and indirectly contributing to growth. *Kinship* refers to developing a trusted advisor and partner relationship with the CEO and other operating executives. And of course, finance must be viewed as a member of the team, supporting and executing to achieve the organization’s objectives.

This article led me to focus on activities that contribute to the firm’s success as a “Partner in Driving Performance and Value.” Throughout my 45-year career, I have found that these value-added finance activities that contribute to performance improvements and value creation are the most important roles the finance team plays. I became a student of financial analysis early in my career and can directly attribute attaining my goal of becoming a CFO in large measure to a strong focus and emphasis on FP&A, decision support, and other value-added activities throughout my career.

I define *value added finance activities* very broadly, as evidenced by the scope of this book. These draw on several academic areas, including managerial accounting, financial accounting, finance, operations and process management as well as new disciplines in analytics, data visualization, and artificial intelligence. Today, the finance team is called on to lead the development of plans and projections, evaluate trends and variances, evaluate complex investment decisions, value and increase the value of the enterprise and acquisition candidates, among many others.

The title of this work is *Financial Management: Partner in Driving Performance and Value*. The term *financial management* recognizes that many “value-add activities” occur in other areas outside the typical FP&A function. This book will emphasize that finance should be a partner with other executives in achieving organizational goals. Finally, finance can and should play a key role in driving overall performance of the organization and maximizing shareholder value.

Even with the broad scope and increasing importance of financial management, there are very few resources available to senior financial managers, analysts, and FP&A departments. The objective of this book is an effort to address that void by providing a comprehensive and practical guide to FP&A and other key finance contributions.

## USING THIS BOOK

The book can be utilized in one of three ways. First, a cover-to-cover read for those deeply involved (or aspiring to participate) in all facets of financial leadership. Second, many readers may peruse the entire book and then focus on specific areas of current interest. Finally, my hope is that the book will be retained for use as a future reference.

This book is organized into seven parts:

- Fundamentals and Key Partner Capabilities
- Financial Leadership in the 21st Century
- Enterprise Performance Management
- Business Projections and Plans
- Planning and Analysis for Critical Business and Value Drivers
- Valuation and Capital Investment Decisions
- Summary and Supplemental Information

### **Part I: Fundamentals and Key Partner Capabilities**

Part I includes a review of fundamentals of finance and key analytical tools. It also covers important FP&A capabilities, including developing models, building analytical capability, and presenting and communicating financial information.

### **Part II: Financial Leadership in the 21st Century**

In Part II, several areas in which finance can provide leadership across the organization, including value creation, strategic planning, supporting growth, human capital management, and technology utilization, are presented. The management challenge, including finance, has intensified in recent years, especially owing to the impact of the Covid-19 pandemic and aftermath. This section includes frameworks to deal with the level of uncertainty and pace of change we are experiencing in business, including monitoring external forces, scenario management, and enterprise adaptability.

### **Part III: Enterprise Performance Management**

Part III includes an introduction to enterprise performance management and best practices in developing key performance indicators and dashboards. It also provides guidance on institutionalizing performance management, that is, integrating it with other management processes. Additional topics include the measurement of innovation, agility, and human capital as well as applying

performance measurement to external forces, including benchmarking and competitive analysis.

#### **Part IV: Business Projections and Plans**

Part IV covers best practices in developing projections and plans. Topics include budgets, operating plans, rolling forecasts, business outlooks, and long-term projections. Special attention is given to techniques to deal with the uncertainty and rapid change that exists in the 21st century.

#### **Part V: Planning and Analysis for Critical Business and Value Drivers**

This section covers techniques for planning, analyzing, and improving on key performance drivers: revenue growth and margins, operating effectiveness, capital management, and the cost of capital.


#### **Part VI: Valuation and Capital Investment Decisions**

Part VI addresses business valuation, value drivers, and analysis of mergers and acquisitions. In addition, the evaluation of capital investments is covered, from basic concepts through advanced topics, including dealing with risk and uncertainty.

#### **Part VII: Summary and Supplemental Information**

Part VII summarizes key points from throughout the book and provides suggestions on improving our ability to contribute as a “Partner in Driving Performance and Value.”

#### **WEBSITE**

A number of illustrative analyses, performance dashboards, and models used in the book are available on the website. These items are identified in the book with a . The dashboards, spreadsheets, and analysis are intended as working examples and starting points for the reader’s use. An important theme of this book is to underscore the importance of selecting the appropriate measures and dashboards. It is very important to carefully select the measures that are most appropriate for each circumstance. Accordingly, most of the dashboards and models will have to be tailored to fit the specific needs of the user.

The spreadsheets contain the data used in the examples provided in the book. In all cases, the input fields are highlighted in blue. The reader can save

these files under a different name and use them to begin developing dashboards and analysis for their specific needs. Using the models on the website requires Microsoft Excel software and an intermediate skill level in the use of that software. Additional information on the use of the website can be found in Appendix A: What's on the Website.

## **GLOSSARY**

A glossary of commonly used financial, value, and performance management terms is included at the back of the book.

—Jack Alexander





# Partner in Driving Performance and Value

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“Try not to become a person of success but rather a person of value.”  
—Albert Einstein

Financial management, financial planning and analysis (FP&A), and other financial business partners (FBPs) play important roles in the overall success of any enterprise. In this chapter, we will introduce the critical value-add activities that contribute to becoming a “Partner in Driving Performance and Value,” and we will preview the contents of the remainder of this book.

## WHAT IS A FINANCIAL BUSINESS PARTNER?

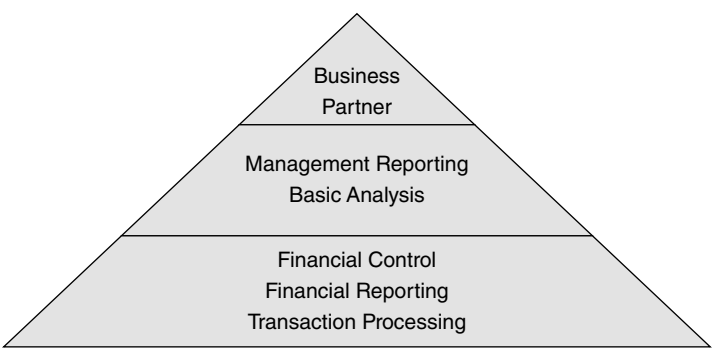
I define an *FBP* as those individuals or teams that support the business in achieving goals for performance, and ultimately, value creation. In this text, I have chosen the label FBP rather than FP&A. FP&A is somewhat limiting and the role of FP&A varies from organization to organization. Much of what we define as a FBP occurs outside FP&A, for example, merger and acquisition (M&A) support, Capital Investment evaluation, financing, and so on.

Finance wears many hats in most organizations. These include varied responsibilities such as transaction processing, statutory compliance, financial control, and financial reporting. While these areas represent important functions and activities, they are not considered value-add activities by most nonfinancial senior executives (until they break!). This book will focus on the value-add finance roles we describe as the FBP. However, finance cannot function at this level unless the core elements of reporting and financial control are effective. If vendors and employees are not paid, or if financial reports

2 PARTNER IN DRIVING PERFORMANCE AND VALUE

are not timely and reliable, then finance must address these to shore up the foundation, enabling contributions at the higher FBP level. This can be conceptualized as a pyramid as illustrated in Figure 1.1, similar to Maslow’s hierarchy of human needs.

FIGURE 1.1 **Business partner pyramid.**



Under the leadership of the CFO, business partner roles may exist across the finance organization as shown in Figure 1.2. Shaded areas represent those areas considered value-add within finance, with the potential to drive performance improvements and create shareholder value.

FIGURE 1.2 **Chief Financial Officer responsibilities.**

Chief Financial Officer					
FP&A	Control	Treasury	Investor Relations	Tax	Other
Monthly Reporting	Monthly Reporting	Capital Structure	Investor Communication	Tax Planning	M&A support
Performance Analysis	Financial Reporting	Cost of Capital	Investor Presentations	Tax Compliance	Real Estate
Financial Plans and Projections	Compliance	Cash Planning & Optimization			Information Technology
Decision Support	Internal Control	Investment Evaluation			Strategic Planning
Scenario Management	Financial Data	Cash Management			Value Creation
		Other			

FINANCIAL ANALYSIS AND ENTERPRISE PERFORMANCE MANAGEMENT (EPM)

A major area that adds value across the organization is financial analysis and enterprise performance management. Figure 1.3 presents the instrument panel in the cockpit of the space shuttle, which represents a great illustration of key objectives of EPM. At a glance, the pilot can get a highly visual report on the

shuttle's altitude, on its attitude, and on every major system in the aircraft. The radar in an airplane allows the pilot to spot and identify potential external threats long before visual contact. At first, the panel appears very complex, but you can bet the pilot knows where every needle and dial should be and the importance of any changes! Pilots compare this information with the feel of the plane, visual observation, experience, and intuition to make adjustments in real time, as indicated, to operate the craft to safely execute the flight plan or mission.

FIGURE 1.3 **Space shuttle cockpit instrument panel.**



Photo used with permission of NASA.

In a nutshell, one of the fundamental roles of finance is the development and delivery of information to run a business and achieve an organization's goals, just as the instrument panel assists the pilots of an aircraft to execute their mission.

### **Key Features from Cockpit Instrument Panel**

1. Real-Time and Predictive Insights.
2. High Visual Impact.
3. Focus on the Important Measures.
4. Provides Insight into External Factors and Environment.
5. Combine with Observation, Experience, and Intuition.

## 4 PARTNER IN DRIVING PERFORMANCE AND VALUE

Our definition and application of the FBP is very broad and inclusive. It includes all activities that assess, plan, improve, and monitor critical business activities and initiatives. EPM is a critical aspect of the management processes of the enterprise. Performance management is closely aligned with, and overlaps FP&A in many respects. Key characteristics of effective EPM include:

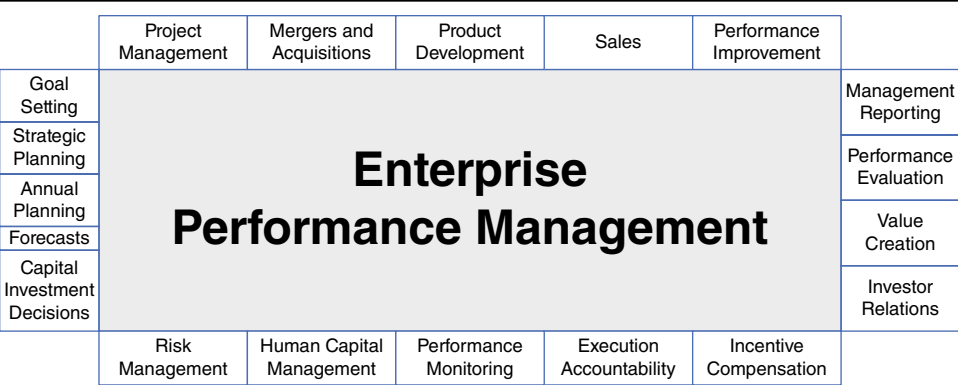
- Achieving an organization's goals and objectives, including strategic and operational initiatives, forecasts, and planned results.
- Projecting and modeling future financial performance.
- Monitoring performance on key value and business drivers.
- Increasing visibility into critical areas of business performance, allowing managers to assign and enforce accountability for performance.
- Providing an effective framework, allowing managers and employees to understand how their activities relate to operating and financial performance, and ultimately, the value of the company.
- Providing early detection of unfavorable events and trends, such as manufacturing problems, supply chain disruptions, competitive threats, and product performance issues.
- Delivering critical information to managers and executives in effective displays or presentation formats that aid in identifying trends, problems, opportunities, and so on.
- Integrating into other management practices in the overall system of management processes that we will call the performance management framework (PMF).
- Identifying, monitoring, and mitigating risks.
- Providing information to managers to run the business.
- Supporting growth.
- Identifying and managing risks and uncertainty.
- Scenario analysis and planning.
- Monitoring progress on critical projects and programs.

FP&A and EPM must be integrated into other management processes as shown in Figure 1.4. Analysts and others involved in EPM must play an active role in the management of the organization. They are not reporters or historians; they should help shape the outcome of the enterprises' efforts.

### Understanding How Decisions Are Made

Since a substantial part of finance's value-add contribution involves developing and providing information and analysis to managers, partners should

FIGURE 1.4 **EPM integration with other management processes.**



develop an understanding of how the human mind receives and processes information as part of evaluating options and making decisions. The analyst bears a responsibility to develop and present findings in an objective manner that reduces bias and the tendency to reach less than optimum decisions.

A primary theme throughout this book is the need to present and communicate business information effectively. This subject is the focus of Chapter 5, “Presenting and Communicating Financial Information.”

**Preview of the Book**

The book has been written to address key areas of financial management from a practical point of view. While theory and technical aspects are included throughout the book, I have tried to incorporate real business applications from my 45-year career in business accounting and finance. Some readers will explore the entire text, while others may dive into a specific topic of particular interest at the time. Where appropriate, I have included cross-references to other parts of the book that cover related material to assist the reader.

Most of the illustrations are Excel-based since nearly all analysts have access to Excel, and it facilitates illustrating key concepts.

The book contains seven parts:

- Part I: Fundamentals and Key Partner Capabilities
- Part II: Financial Leadership in the 21st Century
- Part III: Enterprise Performance Management (EPM)
- Part IV: Business Projections and Plans
- Part V: Planning and Analysis for Critical Business and Value Drivers
- Part VI: Valuation and Capital Investment Decisions
- Part VII: Summary

**Part I: Fundamentals and Key Partner Capabilities** Part I builds a foundation for effective planning, analysis, and performance management. It includes a comprehensive review of financial statement analysis and presents analytical tools that can enhance the effectiveness of FP&A. For many finance professionals, Chapter 2 is primarily a review so a quick perusal of this material may be appropriate. This material serves as a foundation for many concepts presented in later chapters.

In order to complement technical subject areas in the book, we cover best practices in developing financial models and in developing analytical capability and other skills to add value as a business partner. Finally, we address a significant weakness in many finance organizations: presenting and communicating business information.

Part I contains these chapters:

- 2: The Fundamentals of Finance and Financial Statement Analysis
- 3: Skills, Knowledge, and Attributes for Financial Business Partners
- 4: Developing Predictive and Analytical Models
- 5: Presenting and Communicating Financial Information

**Part II: Financial Leadership in the 21st Century** In Part II, we present several areas in which finance can provide leadership across the organization, including value creation, strategic planning, supporting growth, human capital management, and technology utilization. This part also includes frameworks to deal with the level of uncertainty and pace of change we are experiencing in business, including monitoring external forces, scenario management, and enterprise adaptability.

Part II contains these chapters:

- 6: Essential Ingredients for Value Creation: Growth and ROIC
- 7: Managing Human Capital and Building a High-Performance Finance Team
- 8: Strategic Analysis and Planning
- 9: The Role of Finance in Supporting Growth
- 10: The External View: Markets, Competitors, and Economic and Geopolitical Forces
- 11: Course Corrections: Business Transformations and Restructurings
- 12: Leveraging and Promoting Technology Investments
- 13: Scenario Analysis, Planning, and Management
- 14: Adaptability: Innovation Agility and Resilience

**Part III: Enterprise Performance Management (EPM)** In Part III, we focus on subject matters traditionally associated with performance management. After introducing keys to effective EPM, we present the best practices in selecting key performance indicators (KPI) and creating dashboards. In order to fully achieve the benefits of EPM, it needs to be integrated with other key management processes. We introduce a challenge to business leaders to focus on *what's important*, not just what is easy to measure. Since performance management should also look outside the enterprise, benchmarking and competitive analysis are also presented in this section.

Part III contains these chapters:

- 15: Enterprise Performance Management and Execution
- 16: Dashboards and Key Performance Indicators
- 17: Institutionalizing Performance Management
- 18: Benchmarking Performance

**Part IV: Business Projections and Plans** In Part IV, we cover best practices and techniques for planning, projecting, and forecasting future performance. In addition to traditional budgeting and operational planning, the implementation of rolling forecasts or business outlooks are also presented. Finally, we cover the unique challenges in projecting performance over an extended time horizon.

Part IV contains these chapters:

- 19: Business Projections and Plans—Introduction and Best Practices
- 20: Budgets, Operating Plans, and Forecasts
- 21: Long-Term Projections

**Part V: Planning and Analysis for Critical Business and Value Drivers** This part presents best practices and illustrations for planning, measurement, analysis, and improvement of key business and value drivers.

Part V contains these chapters:

- 22: Revenue and Gross Margins
- 23: Operating Effectiveness—Costs and Expenses
- 24: Capital Management and Cash Flow—Working Capital
- 25: Capital Management and Cash Flow—Long-Term Capital Assets
- 26: Risk and the Cost of Capital
- 27: Capital Structure and Financial Leverage

**Part VI: Valuation and Capital Investment Decisions** Part VI presents analysis and evaluation of critical business decisions, including capital investment decisions, techniques for valuing a business and analyzing value drivers. This part concludes with techniques to value a business, and the planning, analysis, and evaluation of mergers and acquisitions (M&A).

Part VI contains these chapters:

- 28: Capital Investment Decisions—Introduction and Key Concepts
- 29: Capital Investment Decisions—Advanced Topics
- 30: Business Valuation and Value Drivers
- 31: Analysis of Mergers and Acquisitions

### **Part VII: Summary and Supplemental Information**

- 32: Summary and Where To from Here?

Supplemental information is also provided, including a glossary, an index, an appendix listing all models and illustrations, and information on the website available to purchasers of this book.

## **SUMMARY**

Financial management and business partners have the potential to add tremendous value to the enterprise beyond simply closing the books and paying the bills. Combining elements of classic FP&A with EPM can unleash significant analytical horsepower that can assist the organization in executing its mission and achieving its objectives.

Before embarking on an initiative to improve the performance of FBPs, practitioners should develop a context based on the company's strategy and objectives, performance, and critical initiatives. This will ensure that the focus of our efforts is directed to critical areas in the organization. Material found in Chapter 3, "Skills, Knowledge, and Attributes for Financial Business Partners" and Chapter 7, "Managing Human Capital and Building a High-Performance Finance Team" will be helpful to this cause.



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Part One

# Fundamentals and Key Partner Capabilities

