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BUSINESS GUIDE

5 Financial Management Secrets CFOs Need to Know

These shrewd finance leaders have been around the block — and we're not afraid to ask them for tips

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In 2001, Rick Bauerly had an idea: Create a different kind of investment company, one that would buy and hold locally owned businesses, giving owners who were ready to exit a third option versus selling to a typical private equity firm or large corporation that might not treat customers or employees well. Thus, Granite Partners was born.

"Our alternative is private and local and long-term ownership, where we buy to hold the companies," said Bauerly, Granite Partners' founder and CEO. "This is an important distinction. We don't sell them."

Granite identifies businesses with owners who see value in this model, have a healthy and happy customer base, operate in an industry with clear opportunity for growth, and have a strong presence in their local communities. It purchases these companies with the guiding objective to help these organizations succeed 100 years into the future.

Obviously, it's selective. It's also eclectic: Granite's holdings include everything from industrial manufacturing to software development to healthcare supplies and services, and it's in it for the long haul with that century outlook.

Which brings us to our first secret.

1. Successful CFOs have North Stars that guide financial management decisions.

Bauerly, for example, focuses first and foremost on the wellbeing of employees and communities. Sounds squishy, right?

Maybe. But the results speak for themselves. Since its inception, Granite has significantly outperformed relevant public market indices and private company benchmarks. Portfolio companies tend to grow revenue significantly once they come under the Granite umbrella.

"And I don't mean by percentages, I mean revenue is four to five times what it was when we invested, and earnings are an even more significant multiple," said Bauerly of one holding. "By focusing on sustainability and 100 years, we make a lot of decisions, small daily decisions or big annual decisions, differently than if you're trying to grow something for three years, or if you're trying to meet quarterly earnings."

There are plenty of valid business guiding principles. Entire MBA courses are devoted to the concept. Maybe it's an emphasis on quality products or services or on operating hyper-efficiently. Heck, even "move fast and break things" is a guiding principle that informs financial decisions.

If you don't know what your company's North Star is, this is where you start. A financial management plan flows from there.

Learn more about how Granite Partners' Bauerly grew his company to a total equity value of more than $1 billion with a lean team that partners with 2,500 employees across 10 portfolio companies.

2. Cagey CFOs are obsessive about FP&A and incorporate business units and operations into extended planning.

Even though the typical finance organization spends about 10% more time and resources on financial planning and analysis than it did a decade ago, according to a recent McKinsey & Co. report, economic volatility is laying bare the shortcomings of teams geared toward quarterly and annual cycles rather than more fluid FP&A.

The firm profiled a consumer products company that created an enterprise dashboard that executives can call up during meetings to gain an up-to-date, end-to-end view of transportation and logistics data. That let the company spot an increase in less-than-truckload (LTL) shipments and act to reduce that metric by 15%.

The savings were significant, but getting there required real-time input from a variety of operational units and a laser focus on business growth, efficiency, and value creation.

McKinsey says next-level FP&A teams maximize use of technology, find and share insights quickly, and carve out a role for themselves as critical partners to the business.

Maybe get your people mugs that say "Always Be Forecasting."

Josh Burwick, an active private technology investor who has served as an interim CFO, says one secret to success is ensuring you dynamically adjust forecasts to account for changes to assumptions, such as higher churn because of a price increase or fewer new customers because of a recession. And, ask lots of questions: In which areas were you accurate? Where were forecasts way off?

"As my grammar-school teacher would say, 'It's not about getting it right or wrong, it's the logic you showed to get to your answer,'" Burwick said. "You will learn much more about your business from inaccurate forecasts than from any that you got right."

A good process to follow:

Plan:
Create scenarios, and decide which factors are critical to watch.

Do:
Execute on your business strategy as you monitor those critical factors.

Act:
Implement the scenario plan most appropriate, and repeat the cycle.

Check:
Do factors begin to hew toward one scenario or another?

Learn More

- **6 Capabilities FP&A Teams Need in 2023 to Drive Business Performance.** Businesses are sitting on piles of data. Uncovering innovative ways to use it to drive success is the job of financial planning and analysis teams.
- **Financial Planning & Analysis (FP&A): Practices, Roles, Responsibilities, and Functions.** The FP&A function is becoming increasingly forward-looking. It's using best practices to focus not only on what happened or what's happening but on why it's happening and what is likely to happen in the future.

3. Savvy CFOs aren't married to the annual budget. In fact, they don't even consider "reforecasting" a dirty word.

Another outsourced CFO, James Vanreusel, CEO of Vanreusel Ventures, says it's sometimes his responsibility to deliver bad news — such as telling department leaders they need to rethink their budgets because the company has wildly diverged from its roadmap.

Is that popular? Not usually. But mid-fiscal-year budget recompilations are a financial management tool that seasoned executives keep in their back pockets, even though recompilations are a burden for not just business leaders but also finance staff.

"That's true even when you're rebudgeting because sales are significantly higher than expected," Vanreusel said. "In those cases, you're not greeted like an angel of doom, and needn't worry about morale and attrition. But still, you're asking for a lot of unplanned work."

His preferred method is a new 6+6 budget that shows six months of actuals and six months of forecasts.

CFO Checklist

Vanreusel says he has five rules he lives by:

1. No surprises! Ever.
2. Constantly stay on top of your assumptions.
3. Calculate your project ROIs to effectively allocate capital.
4. Review your goals daily.
5. Daily ask, "Where's the risk?" and "What can go wrong?"

There are two ways to approach financial management when actuals and budgets diverge significantly.

Scenario 1, tactical reforecasting: The board-approved budget remains untouched. The CFO tells each department head, "We need your plan to cut 5%, along with any worries you have about what that might do to growth."

Scenario 2, strategic rebudgeting: If there's a large swing from expected sales, say up 50% or down 30%, the CFO rebudgets because something has strategically changed. It's no longer just investing more or less in the same areas, but an actual deep dive into where the highest ROIs are now coming from.

The reality of the moment dictates which you'll do. Are sales changing substantially? Then it's Scenario 2. Are we just trying to batten down the hatches because we're worried about a Fed-induced recession? That's Scenario 1.

"If you're doing a 6+6 right, stakeholders across the organization will question all assumptions," said Vanreusel. "It's very hands-on, to the point of being invasive. Watch out for superficial efforts and back-channel complaints. These will need to be managed if the rebudgeting effort is to be successful."

4. CFOs who excel at financial management don't stay in their lanes. Or any lane.

Maybe we should have done this earlier, but let's define the term:

> "Financial management is the practice of handling a company's finances in a way that allows it to be successful and compliant with regulations."

That's broad, and it should be. Solid financial managers help their companies in five main ways, and all of them may require CFOs to make moves that could be perceived as stepping on toes. Data says other execs want CFOs more involved with ongoing operations, so there's support for leaning in.

Learn More

- **What Are Flexible Budgets? 4 Best Practices.** Flexible budgets are essentially budgets that can be adjusted depending upon revenue and cost changes throughout the fiscal year, accounting for expected unpredictability.
- **5 Best Practices to Perfect Rolling Forecasts.** Economic volatility has put the shortcomings of traditional budgeting methodologies on full display. The smart money is moving toward rolling forecasts as a better way to predict business performance — and get finance in line with sales, marketing, and production.

Big financial management goals are to:

1. Maximize profits: Gather more data to provide insights on, for example, rising costs of raw materials that might trigger an increase in the cost of goods sold.

   Uncomfortable conversation: "We need to cut this supplier loose. I know it's been a good partner for years, but these price increases are unsustainable for our business. Talk to them, and meanwhile, explore other options."

2. Automate more. You can both improve finance data collection and reduce the human costs of certain processes with automation.

   Uncomfortable conversation: "We need to redirect money from headcount to technology, even if that means giving up on making that hire. Let's get some tech in here so we're less dependent on manual processes."

3. Track liquidity and cash flow: Make sure the company has enough money on hand to meet its obligations.

   Uncomfortable conversation: "The sales team is giving way too generous terms and discounts. Money we get in two weeks is worth more than money we get in two months. Rein it in — net 15 and no more than 10% off list without my approval."

Note that the nature of sales often makes this an area where CFOs tread lightly.

"In many companies, sales has long been a kind of 'black box,'" says Frank V. Cespedes, senior Harvard lecturer and author. That needs to stop. The sales team drives revenue, and unless you set rules that make sure there's good margin with that revenue, salespeople will do what it takes to make the sale.

The CFO must work with sales leaders to create the right incentives to sell the right products. Financial management success requires that correlation be made clear.

4. Ensure compliance: Keep up with state, federal, and industry-specific regulations.

   Uncomfortable conversation: "I know we're applying for a new line of credit, and yes, recording as revenue the deal that's 'definitely' going to close next week will look good. But we're not going to overstate revenue."

   The CFO is often the "conscience" of the company, and it's critically important to take that seriously, says Jack McCullough, CFO Leadership Council founder and president.

   "Who is the most trusted executive in your company?" McCullough said. "In most cases, it's the CFO."

   If that means being the ethics police, so be it.

5. Develop financial scenarios: These are based on the business's current state and forecasts that assume a wide range of outcomes based on possible market conditions. A big factor: How much do you trust sales estimates?

   Uncomfortable conversation: "Estimating 40% growth in B2C sales a month after we launch a new product line is what's called 'irrational exuberance.' I appreciate the optimism, but let's get realistic."

6. Manage relationships: Dealing effectively with investors and the boards of directors.

   Uncomfortable conversation: "We need to understand who on the board is really good at numbers and finance and willing to tell it like it is, and partner with that person versus the ones telling us what we want to hear over dinner and cocktails."

   Burwick says three factors prevent boards from providing the support and direction their portfolio companies need to succeed.

   "The first is a lack of diversity," he said. "Despite recent progress, most boards still consist of gray-haired men with CEO and investment backgrounds. Second is a failure to communicate regularly, both among board members themselves and with a diverse group of company leaders. And finally, the size and composition of a board may not be the right fit for a given company. Bigger is rarely better."

   Point is, not much is off limits for CFOs. Setting prices, "firing" unprofitable customers, deep involvement with boards, and enforcing ethical guidelines across departments.

   Top financial managers make their own lanes.

5. The best financial managers surround themselves with skilled people and top technology.

An excellent controller and capable financial management software are table stakes. From there, smart CFOs are not only comfortable letting other employees take the lead in areas where they have greater expertise, they actively encourage it.

"I think you have to have a ton of self-awareness in any leadership position," said Drew Cook, CFO of direct-to-consumer clothing retailer pact. "You need to know what you know and what you don't and be prepared to take a step back if it's not something you're great at."

Cook advises finance heads to actively seek ideas from employees at all levels and then make it a point to publicly act on suggestions to show it's not an empty exercise.

Learn More

- **5 Ways Finance and Sales Should Work Together Toward a Healthier Company.** As the finance department becomes a central source for data, its interactions with other departments, particularly sales, can drive improvements.
- **Most Boards Are Dysfunctional. Here's How to Fix That.** Here are the three reasons boards fail to steer properly — and strategies to make sure your company doesn't suffer.

And don't stay internal. Top CFOs credit mentors and professional groups for helping them succeed and advise those just coming up to start identifying people in their networks with a diverse range of backgrounds who can serve as sounding boards. McCullough launched the CFO Leadership Council, a professional association with chapters all over the country that works to empower senior financial executives to realize success in their careers, as a passion project. It's helped hundreds of finance executives reach their potential.

Another major area cited is IT and data wrangling.

In May 2017, The Economist's cover depicted oil rigs that looked like office buildings and stated: "The world's most valuable resource is no longer oil, but data."

The oil-data analogy has been popular in the halls of Wall Street, Silicon Valley, and Washington ever since for good reason: Proper collection and analysis of data can reveal almost any information and generate insights that are important to a business.

Technology can help CFOs deal with what Cook says will soon become a volume of data that's unmanageable without a robust system, like NetSuite ERP plus Advanced Financials, that can not only automate manual functions but provide reports that consolidate key data into actionable insights.

The Bottom Line

On a tactical level, financial management procedures govern how you process daily transactions, perform the monthly financial close, compare actual spending to what's budgeted, and ensure you meet auditor and tax requirements.

On a more strategic level, financial management feeds into vital FP&A and visioning activities, where finance leaders use data to help line-of-business colleagues plan future investments, spot opportunities, and build resilient companies.

CFOs who are rock-solid financial managers have one big thing in common: Numbers-backed insights are a big piece of what has made finance chiefs so influential in their organizations.

They have access to and can interpret data and reports with an ease and confidence few peers can match. The key now is to apply those abilities to all aspects of the business — and there is ample opportunity to do so.

Learn More

- **Financial Management Explained: Scope, Objectives and Importance.** In business, financial management is the practice of handling a company's finances in a way that allows it to be successful and compliant with regulations. That takes both a high-level plan and boots-on-the-ground execution.
- **The Starter Guide to Using Data Analysis in Your Business.** Many understand the importance of data in their businesses — they just aren't adept at using it.
- **Using Data Analytics to Make the Leap From a $10 Million to $50 Million Company.** Data is the global economy's most valuable resource — and can offer a big boost to small businesses.

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