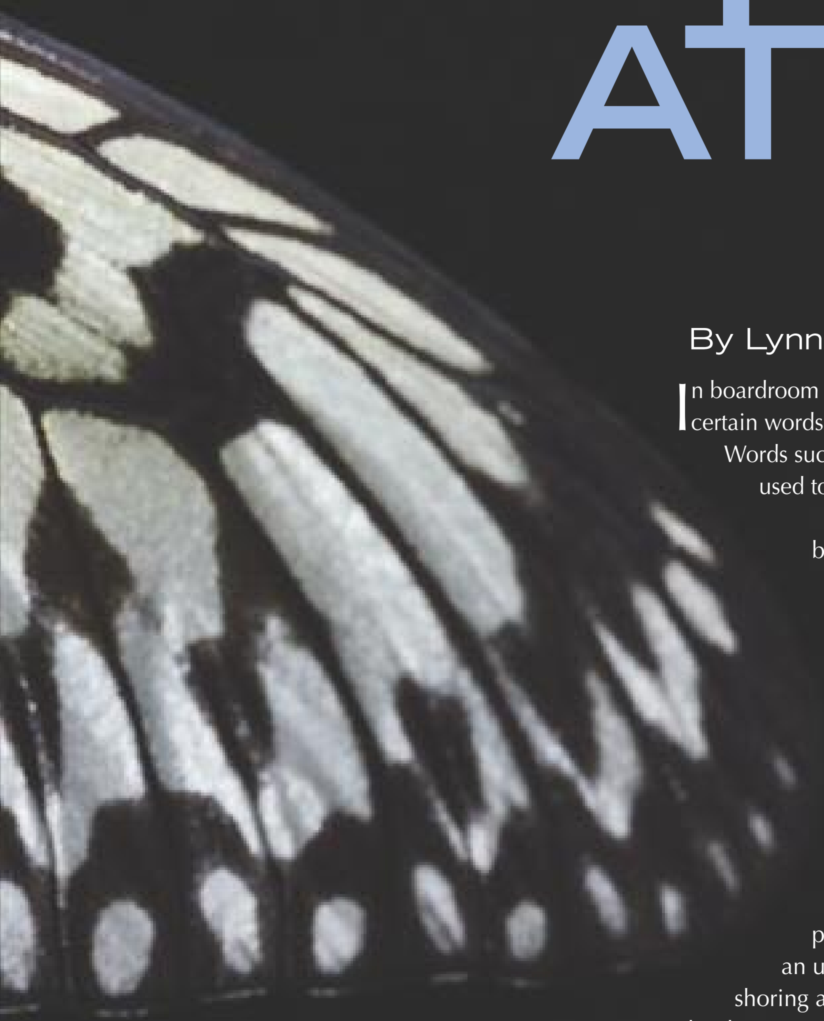
CPE Learning MODULE

This month's feature article is the required-reading for FERFPros "Xxxxxxxxxxxxxx Xxxxxxxxxxx Xxxxxxxxxxx Xxxxx XXXX" [Segment #1 of FMN-October 2013]

ferfpros

POWERED BY SMARTPROS®

The Financial Executive's Role in Influencing Business TRANSFORMATION



By Lynne Doughtie and Steven Hill

In boardroom and business meetings conversations containing certain words and concepts are appearing with great regularity. Words such as "dynamic," "complex" and "disruptive" are used to describe the current state of flux of the economy. Concepts like "market shifts," "regulatory and tax burden", "innovative capacity" and "risk optimization" capture some of the many uncertainties that are influencing key decisions about near and long-term strategies.

This conversation has been shaped by years of global economic change — both good and bad. Five years after a global economic downturn, recovery is inconsistent from nation to nation and quarter to quarter.

Emerging markets around the world — though representing significant opportunities for companies from a market, production and supply perspective — are presenting new challenges, with an uncertain future for what had been consistent off-shoring and growth stories in places like China and India. The downturn has also caused many governments around the globe to refocus and expand their regulatory stance on business oversight

Though the past decade has not been, the turmoil has given financial executives first-hand experience with many of the drivers of transformation.

and taxation. In addition, political divisions have also influenced regulatory and policy changes, affecting growth in the United States and the European Union, while political shifts in the Middle East have created uncertainty around markets and supply chains. Consider also that leadership changes and demographic challenges from aging populations in China and Japan have affected current and potential future regulatory policies in those regions.

All the while, technology continues to evolve, opening up the possibilities and pitfalls of cloud environments, social media, data and analytics and wide-scale mobility. These and other technology changes are fostering the creation of entirely new industries and enterprises at the same time that they redefine how existing businesses operate and influence customer choices.

The biggest question of all is: How can a business translate all of this rapid change into a competitive advantage and, ultimately, a sustainable profit growth profile? In the face of so much change happening at so fast a pace, today's leading businesses are challenged to develop an operating model that will allow them to meet and exceed growing market demands.

But even beyond just keeping up with change, many businesses have opportunities to use the economic uncertainties, regulatory changes and disruptive technologies to their advantage. Those seeking to find that advantage are focused on "transformation" to drive profit growth and evolve and build for the future. In fact, 93 percent of 910 executives at U.S.-based multinationals and asset management firms said their companies were in some stage of changing their business models, according to a KPMG survey due to be released this fall.

The biggest question of all is: "How can a business translate all of this rapid change into a competitive advantage and, ultimately, a sustainable profit growth profile?"

The goal of such transformation is to create an operation that is not only aligned with strategic objectives of the moment, but is also innovative, agile and responsive to change. Businesses that undertake transformations are better focused on their customers, and better equipped to stay ahead of current competitors, as well as to new challenges and opportunities.

Transformation as a Competitive Advantage

Transformation is about making comprehensive changes to the business at a time when incremental shifts are not sufficient. Businesses are challenged to think holistically, to develop operating models that will empower them to respond to current pressures and translate change into a competitive advantage.

While the presence and persistence of change are obvious, finding the right response is a more significant challenge. To transform an operation into a model better suited to today's demands, C-suite executives have to ask a wide range of pressing questions, such as:

• With the changes in markets around the world, impacts on costs and supply chains, opportunities for mergers or acquisitions and emergence of innovative and disruptive technologies, what will the business look like in the next five years?
• With access to information growing each day, and the demand for goods and services evolving, how will customer needs and wants change in the future?
• Who are the competitors today, and who will be competitors in the years ahead? Is this a space where existing or new technology lowers the barriers to entry? Stacked up against competitors, what are my company's greatest vulnerabilities and what are its greatest strengths?
• To stay innovative, cost-effective and ahead of the curve, what will be the most effective operating model in the years ahead?
• How does the company manage its increasing risk, optimize its global tax position and address regulatory changes?

Many of these are questions that executives did not need to ask 15, 10 or even five years ago. They are now essential considerations in a world where information moves faster and is more accessible than ever, where supply chains are far flung and complex and where increased regulatory influence is altering the playing field for many industries.

For example, financial services organizations are currently managing a highly charged regulatory landscape, lost revenue and rapidly changing customer preferences. This difficult environment has thrust industry participants into a transformation journey. They are overhauling their operating models with the overriding goal of reducing costs to improve efficiency ratios and aligning business practices with new regulatory agendas.

In many cases, industry leaders have moved aggressively to automate manual processes through workflow solutions and to optimize infrastructure such as physical locations and aging technologies. The industry has been challenged with promoting agile processes exposed through cross-customer channels and moving toward real-time posting and analytics to enable greater cross-sell and share-of-wallet initiatives.

At the same time, financial service providers have been seeking ways to simplify products and service attributes for better customer transparency.

These are examples of some of the challenges arising in a single industry, and are a small measure of transformations happening in multiple sectors.

Four Drivers of Transformation

To help narrow the issues happening across the economy, KPMG analysis has identified four key drivers of transformation: Economic Forces; Regulatory Requirements; Customers and Competitors; and Disruptive Technologies.

• ECONOMIC FORCES include factors like slow growth and the need for cost reduction, challenges that many businesses still face as the impacts of the global downturn continue to be felt and as recovery happens in fits and starts around the world. Other economic concerns include new sourcing and business models and an increase in mergers and acquisitions. According to the most recent data from KPMG's International Global M&A Predictor [DEFINITION OF THIS IS NEEDED], the appetite for acquisitions is poised to increase in the years to come, especially in the U.S., where corporate balance sheets are flush with cash and credit markets are improving.

• REGULATORY REQUIREMENTS. Companies are facing rapid change, increasing scrutiny and transnational considerations. Political stalemate in some markets, and unrest in others, is fostering a need to predict, prepare and respond with agility to changing regulatory, tax and trade requirements.

• CUSTOMERS AND COMPETITORS are forcing businesses to confront low-cost market entrants, changing preferences, changing channels and increasing transparency. Social media networks and technology are making brand protection more difficult and allowing customers to voice demands in unprecedented ways. Among the 910 companies surveyed, customer demand was the most commonly cited trigger for transformation among 33 percent of respondents, while 30 percent cited domestic competition as a transformation driver.

• DISRUPTIVE TECHNOLOGIES include social, mobile, analytics and cloud. Indeed, cloud and mobile are expected to be the most disruptive technologies in consumer and business markets over the next three years, according to another recent KPMG survey of more than 800 business leaders, representing startups, midsized and large enterprises, venture capital firm and angel investors from around the globe.

Data and analytics are expected to play a greater role as breakthrough technologies are developed over the same timeframe. Nearly a third of respondents in the transformation survey cited technology as their transformation motivator.

With all of these factors to consider, businesses are expected to spend as much as $30 billion on transformation in the coming years.

Transformation and the Financial Executive

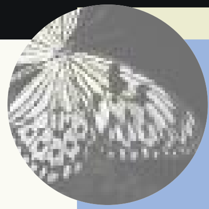
In considering and undertaking a transformation strategy, financial executives can help provide the CEO and other leadership with the vision and pragmatic approach to help the organization move forward.

In fact, chief financial officers are uniquely prepared for today's issues.

Though the past decade has not been easy on financial executives, the turmoil and upheaval in markets, technology and compliance management have given financial executives firsthand experience with many of the drivers of transformation. The tactics that CFOs applied to moving their companies forward during the recent recession may provide the foundation they need to drive future strategy and corporate culture changes.

For years, CFOs have been working to develop processes and models that deliver faster, more accurate and more insightful analysis and reporting while also ensuring compliance and managing risk. One or all of these factors might be driving the need for transformation in an organization, positioning the CFO to contribute significantly to those efforts.

For these reasons and others, the CFO is often a key influencer of transformations across a business. Financial executives can partner with the CEO,



Business transformation is about making comprehensive changes to the business at a time when incremental shifts are not sufficient

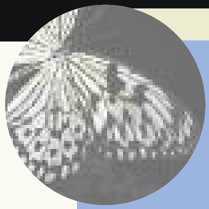
division president or functional leaders to enable transformation strategies that deliver quantifiable and sustainable results. Even the most ambitious transformation vision is of limited use without a workable path to implementation.

In addition, no transformation effort is worthwhile if it does not deliver financial results. The CFO is critical to measuring success in a business transformation and tying results to the actual performance of the business.

As with any large strategic undertaking, transformation is a journey. Any effort to innovate and implement a new target operating model should be envisioned and implemented as part of an ongoing process.

The goal of business transformation is not to move from one static place to another, but to make changes that will prepare the organization with the tools and skills it needs to effectively manage ongoing change, to adapt in the future and to turn the challenges of a dynamic business environment into drivers of sustainable profit growth.

This is true even when the business is responding to a specific business issue. Maybe a particular industry has just seen the introduction or proliferation of a disruptive technology, such as cloud or a new data analytics capability. Maybe the greater access to information through social media is leading to higher expectations of value from



Financial executives can partner with the CEO, division president or functional leaders to enable transformation strategies that deliver quantifiable and sustainable results.

clients or customers. Maybe the services and solutions the company has traditionally provided are now being delivered in unprecedented ways through new delivery models, like mobile capabilities.

Transformation needs come in different shapes and sizes, and there is no one-size-fits-all approach. A variety of needs must be met with a variety of different tools. But with that in mind, any effective journey to transformation begins at the intersection of strategy and tactical enablement. Vision is important, but visions have to be translated into implementable practices.

As a critical first step, it is vital to ensure that individuals in the C-suite agree on the vision, strategy and goals of any transformation. An enterprise change requires the support of leaders with an enterprise perspective, who must coalesce around a specific business objective and execute together, breaking down silos and driving change at all levels and across key functions.

The alignment of the organization is critical: 44 percent of companies in the above-cited survey said their executive committee decides how to prioritize business transformation initiatives under consideration. Leadership engagement is essential to preparing an organization for change and seeing it through, to breaking down silos and ensuring that all perspectives are considered when making decisions, and to collaborating on the many steps that foster a successful transformation.

Implementing Solutions and Measuring Value

Transformation involves big changes. Those changes, however, are most often the culmination of many small, incremental steps successfully put in place over time. Implementation requires prioritization of these steps, tackling them in a manageable way and measuring progress against stated goals. It is also critical to maintain flexibility so in order to make necessary course adjustments along the way.

With a focused vision, it is important to bridge strategy and execution. This is where the "big picture" is broken down into brush strokes. Where does the transformation begin and what are the steps that follow until the company has reached its target operating model and value realization? What is the timing horizon? What are the investments that need to be made to improve and expand? What are the steps for continuing the journey once today's goals have been met?

It is critical to move step by step, to unwind complexity, and to understand the ripple effects of each action as the vision is operationalized.

It is also important to make room for innovative changes — those that truly differentiate an enterprise from its competition to create sustainable competitive advantage. In this day and age, it is not good enough to just keep up with best practices. Leaders must cultivate and implement an innovation culture that adds unique sustainable changes to the traditional best practice or cost-optimization approach.

Strong implementation also requires bringing insight to focus the vision. Any transformation effort has to start with customer expectations: What do internal or external customers ultimately value?

Another major consideration is the prospects for technology's role in the business transformation. Technology is often the catalyst for new innovations in product and practice.

Multiple additional elements are key to a successful transformation implementation. An organization's structural and functional components, its history and the perceptions of change efforts and how transformation is likely to affect people and culture will need to be considered. There will be a need for governance mechanisms to be in place at different levels, and possibly in different geographies, to successfully implement a transformation.

It is also important — at the outset of the journey — to recognize how the full ecosystem of capabilities can help achieve an organization's goals. The constant rate of change occurring in today's business environment requires a deep and current knowledge of each component of a transformation effort — including market dynamics, regulatory rules, technology advances, operational practices and program implementation techniques.

Having the right internal capabilities and outside advisers working closely within a program governance model is important in developing and executing on the optimal transformation strategy and realizing maximum value and return on investment.

Last, but certainly not least, is integration. It is absolutely necessary to break down the traditional, siloed operations that are common in many organizations and that can be particularly resistant to change during organizational evolutions. Transformation cannot happen successfully if there are barriers between interrelated areas of an organization.

Building a new target operating model necessitates the participation of each part of an enterprise, even in those areas that are not driving change. It is essential to ensure that major transformations are integrated fully into the current and future goals of an organization, strengthening every part of the operation, and serving as an example of how to evolve across the company.

As with any initiative, in transformation it is important to find ways to measure the value of the steps being taken and the changes being made. This is an area where the financial executive's role is critical.

Being able to accurately quantify the return on an investment in transformation is important to ensuring progress over the long term, supporting efforts that may require additional time and resource, and correcting course when the desired results are not being achieved.

Measuring value requires imposing a discipline and objectivity around understanding the economic value drivers of a transformation strategy. Without that discipline, it is possible for a transformation to lose focus and move in directions that don't support the strategy or serve the ultimate interests of the company.

Measuring value is also essential for the future. In addition to substantiating transformation efforts underway in the present, measuring value helps justify and shape future transformations. Without a clear return on investment, it can be hard to mobilize an organization to take on change; and undertaking a transformation without demonstrating measurable value is almost certain to harden attitudes against the ongoing change that is necessary to continue strengthening a business.

Continuing the Journey — A Pragmatic Approach

For many enterprises, leadership in the current economy is going to require more than a handful of small tweaks or a few course corrections here and there. Success is going to be defined by innovative, whole-scale transformation and making changes that impact all or large parts of organizations. That is how businesses can improve operating performance, shift their focus to emerging opportunities that haven't been considered befor, and meet a range of new demands from their customers and regulators.

Transformation is about institutionalizing a better way to manage future innovations and fostering the discipline and the confidence to create change. The true end game is to master disruptive forces, rather than be subject to them, and to translate today's many economic shifts into value producing strategies and competitive advantage. A successful approach to business transformation brings together a broad perspective of the opportunity and its impact with a pragmatic approach to defining actionable steps. Identifying and executing on significant innovative opportunities with pragmatic action steps that will work within the organization at all levels can put iton the path to sustainable business advantage.

It will provide a clearer vision of the future, helping the company to thrive in a world where market dynamics are constantly in flux.

This requires flexibility, not rigidity. It is the product of creating and maintaining responsive business processes and infrastructures that enable the organization to not only respond to change, but to anticipate shifts before they happen.

There will continue to be market shifts and uncertainties. New partnerships, new interactions across global networks and new markets opening up will continue to change the way businesses grow and succeed. Some technological innovation will allow other organizations to step neatly over the entry barriers that have surrounded markets for years or even decades. Disruptive forces will continue to assail the business and demand new adjustments following those that were just made.

There is no end to the need to adjust, which is why success goes beyond simply reaching an immediate goal. An effective business transformation strategy can ensure that organizations are well prepared for the next disruptive force — and proactively equipped to take advantage of it.

Where Are You on the Transformation Continum?

6% Assessing the need for business transformation

27% Planning a transformation initiative

29% Started the implementation of transformation

17% Completed at least one major transformation initiative

14% Have completed several major transformation initiatives

7% Not considering any business transformation initiatives

Lynne Doughtie is vice chair – Advisory and Steven Hill is vice chair – Strategic Investments at U.S. audit, tax and advisory firm KPMG LLP.