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## Challenges for Financial Managers in a Changing Economic Environment

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### Abstract

The fast changes and challenges that took place in the economic environment in the last years broadened the role of financial managers. If their basic responsibilities were linked mainly to financial reporting, financial planning, capital budgeting, capital structure, nowadays a stronger strategic dimension defines the role of financial managers. In addition, an important role is given to the financial manager in communicating professionally not only to the investors but also to the board.

The aim of this paper is to give an overview of the challenges that the current economic context is bringing to the finance function and to present how the role of the financial managers is changing alongside with a transformation of the finance function.

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### 1. Introduction

Changes in the macroeconomic environment have an impact on how businesses operate and in consequence there are changes in strategies and priorities and in the way the departments have to adapt. The more complex the economic system, the more complex the businesses, the more complex the interaction between economic players in a global economy, and the more uncertainties one has to face in these turbulent times, the more complex the role of managers become, including the role of financial managers. There is an interest in understanding how the finance function adapted to these complexities and uncertainties and how companies’ boards and CFOs have approached these challenges by adapting the structures of finance departments and the mix of skills they chose for their teams.

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The uncertain global markets put new demands on the finance function. “Finance must support flexibility, scalability, and responsiveness to a multiplicity of global opportunities and challenges” (Axson, 2012).

The downturn forced companies to increase efficiency, to make cuts wherever it was possible, learn to be more productive, but by now the only alternative for profitability is growth: entering new markets in an uncertain economic environment. To face this changing times, there is a tremendous need to have appropriate skills, new skills, especially for those who manage the finance function in companies. It is vital for companies to have a strong guidance from the finance function to navigate in turbulent times.

## 2. Challenges for the finance function

Many studies were made, most of them being based on interviews with important CFOs that shared their experience in transforming the finance departments in order to better respond to the companies needs in addressing the challenges.

ACCA (The Association of Chartered Certified Accountants) and IMA (Institute of Management Accounting) initiated a series of discussions about the future of the finance function and the future role of CFOs. In their 2012 report on *The changing role of the CFO* it was synthesized the challenges that the finance function has to face in the future:

- Regulations: the more complex and uncertain the economic environment is, the higher the speed of regulatory changes, the higher the need to harmonize regulation across borders. This gives additional roles to the CFOs in order to comply with all regulations and to have in the finance departments the professionals that can cope with the regulatory changes. They also have to have the capability to influence the policy and the regulatory process on behalf of their businesses.
- Globalization: as businesses become global, CFOs have to have a global perspective and experience. They have to understand how their business can operate in different cultures, regions, in different regulatory context in order to provide a valuable input of the finance function into the overall business while expanding in new markets.
- Technology: the finance function has to be in the centre of a data revolution. On one hand there is far more information available that should be collected and processed, on the other hand more complex software to process the data is available. More effective business can be in place once the finance function is using properly the available technology in order to gather, organize and standardize data. Technology will reduce the time spent on looking for data and will give more time in connecting information, providing valuable input in the decision making process and explaining the impact on the business. There is a great opportunity in these turbulent times in using the huge data and the tools to give insight for the further development of the business.
- Risk: the role of the CFO is no more only about cost savings. One of the challenges for the CFO becomes risk management. In a highly volatile environment, CFOs have to be able to approach in a proactive way the diverse risks in order to safeguard the business assets, to prevent poor behaviour that can erode value, to ensure the right policies in what concerns investments, cash availability and shareholder return. The classical balance risk-return is critical in this fast changing environment.
- Transformation: the transformation of the finance function is at two levels. First is related to outsourcing and shared services taking into account the more complex environment and the need for diversified skills. This brings more risk to the business that has to be carefully managed. Second is related to the remaining finance function that should more concentrate on more effective analysis.
- Stakeholder management: the financial manager has not only to prove finance leadership and controllership but to be a strategic partner to the CEO. The senior finance executives are part of the top management team and they have to bring their input in order to help for better strategic decisions. The CFOs have to have good communication skills while they have to communicate not only to investors, banks or financial experts, but in an accessible language to clients, media and the board members.
- Strategy: the financial manager has to connect the finance specific activities and analysis outputs to the realities of the business helping in the strategy formulation and implementation process. The financial managers have to equally balance numbers and strategy. The financial manager has to make a step forward from analysing the past performance and forecasting on the short term to a long term view on the development of the business.
- Reporting: financial management is no more only about achieving financial goals outside sustainability parameters. This includes social and environmental objectives in addition to the traditional economic ones. This is changing

consequently the way decisions are made and performance is measured. There is a triple bottom line reporting: measurement and reporting of performance on social, environmental and financial metrics.

- Talent and capability: many challenges for the CFO in a global context – diverse skills needed in order to respond to a more complex finance function, operations that are developed abroad imposing working with talents from different cultures, incorporating virtual teams in the context of advanced technology. In these conditions, even the profile of a CFO is changed from a specialist to a person with much broader view and skills.

A 2011 KPMG International report on Transforming Finance states that the last decade wasn't easy for CFOs due to "erratic markets, disruptive technologies and a complex web of new regulations and compliance issues" that imposed a redefinition of the role of the finance function in the organization. It is no more about "collecting, paying and reporting", but about "deliver faster, more accurate and more insightful analysis and reporting while appropriately managing risk and reducing cost".

Being flooded with information, the finance departments face an imperative change in order to narrow the information gap, the gap between the information they can access and analyze and the one they need in order to make decisions. The need for more intensive information can be solved through the available technology and sophisticated analysis software. Technology is necessary for improving analysis and reporting but it is not sufficient. There is a strong need for talents with analytical skills, highly trained, that have a general business view, and in many cases MBAs graduates or professionals that worked in banks and financial services firms and that were dismissed during the financial crisis represent the solution for the finance department. But improving technology and IT software that can offer more accurate and deep information for strategic analysis requires a lot of investment from the part of the company. This brings also transformation within the finance function, by creating a stronger link with the IT, and in some companies, even by including the IT function within the finance department.

CFO Research Services and KPMG International made several studies on the transformation of the finance function. They interviewed senior finance executives from global companies to understand how finance functions were transformed and what will happen further. The role of the CFO changed from dealing with the past to give financial advice to look to the future for shaping a sound business in a challenging environment: more complex businesses, a need for more and better information on market conditions, need for more control of risks, fast changing rules and regulations. Finance department should become a contributor of value, not only an observer of the managerial decisions impact. According to the CFOs interviewed by CFO Research Services and KPMG International the finance professionals have to provide useful demographic, market or other data alongside with conventional planning and financial reporting in order to offer strategic advice to the companies' boards.

The CFO Research Services and KPMG International report (2012) contains also some keys to a successful finance transformation that include:

- obtaining a strong commitment for transformation from the CEO and the board;
- translating data and analytics in a business language to be easy to be used by the decision makers;
- recognizing that there is always competition for resources, especially IT resources, and the finance department has to be prepared to make a case why it needs these resources

But the most difficult change the finance function has to face is in communication, both within the finance department and with the businesses. Senior finance executives consider that it is the finance role to convince business leaders that the finance department should not only evaluate past financial performance but get involved in an active way in strategic investment decision, allocate more efficient and effective resources and drive value creation.

### **3. The complex role of the CFO**

The finance function has to make a larger contribution to how the company's departments perform. In fast changing environment, companies need fast and reliable information in order to adapt and make better decision. Providing high-quality analysis, more quickly and in more detail predictions in a constantly changing, volatile economic environment is the new role for the finance function in its active participation in the decision making process. Successful organizations require their CFO "to have vision to look beyond the core functions of finance" and "to use their financial acumen and insights to drive new value and higher levels of business transformation and performance" (Boyle et al., 2009).

In this context the human resource of the finance department has to have an appropriate mix of knowledge, skills and competences, with a higher component of capabilities in strategy, operations, and sophisticated analytics.

A 2009 McKinsey Global Survey Results on How finance departments are changing find that the companies were slowly adapting their organizational structures to comply with the pressures of the economic crisis. Still CFOs spend much more time on critical areas that arise during economic crisis: financial planning and control, risk management, strategic planning. Many companies are increasing the role CFOs play in strategy, risk management and performance management.

According to Axson (2012), to play its strategic role CFOs must excel on several areas: balance cost control and growth, implement robust performance management, unlock the latent potential of finance talent.

The evolutions in the economic environment and the more complex role of the finance function, forced a transformation of the finance department by splitting it into two distinct groups of activities : one routine, transaction-oriented and the other one high-value analytic and strategic. This makes it more difficult for professionals aiming to develop a career in finance. If until now people could enter the department and learn to master from transactional activities to more sophisticated ones, nowadays senior finance executives look for talent with more complex skills: accounting and auditing is no more enough, more MBA graduates are preferable in order to have a strategic overview over the development of the industry and the growth opportunities of the company, communication and project management skills, IT skills to use sophisticated software, mastering a couple of languages and having an international perspective, both Western and Asian.

In order to make a difference in a very competitive environment, the CFO needs more than technical capabilities . He needs to make a difference in the CEO's team - the team that is running the business. The CFO has to understand how the company works and to provide to the other decision makers the information they need in a way they understand. Many people have access to a lot of information. But one should be able to select, to make judgments based on experience and strategic priorities of the company. Once data processed the CFO has to be able to express in simple words what is behind the complex data analysis the finance department is making available. They have to bridge the language barrier, the technical vocabulary the finance professionals use, in order to be able to contribute to value creation in the company. Collecting data, analysing and interpreting the data is important but not enough. CFOs have to be able to well explain to other departments and board members what is behind the numbers.

Leading the finance department on one hand and being part of the senior management team on the other hand, a CFO should be able to cope with these challenges: in one team they lead in the other they are a member.

The CFO should be able to select a team with multiple skills. The work is much more complex, huge data should be processed so that no one single person can have the knowledge and skills to do it. CFOs have to rely on their team. With the input provided by the finance team, the CFO should work on the strategic development of the company with the CEO and other board members. Making their teams work is not easy. Putting different competent people together in an effective way is not possible without establishing rules in how to communicate, how to make decision, how to evaluate performance and how to manage conflicts.

In order to make better decisions, one has to put in place better processes. The better the process is designed the less biases will be in the decision making process. The strategic role of a CFO is to ensure that what weigh more in the final decision are facts and not individual biases (Huyett and Koller, 2011). High quality decision making processes are those in which debates take place, where ideas are challenged by somebody else perspective. And the role of the CFO is to facilitate and to improve the quality of such debates.

But the CFO has to be a member in the CEOs team. Often the senior managers compete for resources, the CEO's favor or for other targets and this evidence is hindering the overall performance of the company. Instead senior managers should collaborate and this can happen only if there are group goals, company strategic goals, as opposed to individual or department goals. The managers' performance should be measured against these overall goals.

According to the studies made by KPMG (2011) the CFO is contributing to the overall performance of the organization based on three core attributes:

Ability to build relationships with stakeholders based on trust: capability to invest, capability to raise funds, ability to manage risk, governance integrity, investor credibility

Ability to simplify financial information regardless its complexity: reliable information, accurate reporting, standardize and automate processes, eliminate duplication, cost efficient

Ability to provide relevant insights for decision making: real-time and insightful information, accurate forecasts, quantitative and qualitative analysis, integrated planning, execute strategy

Considering the current challenges, the profile of the CFO that best suits the needs of companies can be described based on backgrounds and experiences they need to have. In 2013, a McKinsey report, Agrawal, et al. (2013), based on a survey of backgrounds and experiences of the CFOs of top 100 global companies based on market capitalization, concluded that there are four different profiles of CFOs (see Table 1). CFOs characteristics should be coherent with the industry context and the strategic plan of the company. As Agrawal et al.(2013) state in their report, the selection of the CFO should be aligned to "the current corporate strategy, the skills and temperament of the CEO, the composition of the senior-management team, the current capabilities of the finance function, and organizational and reporting structures".

#### 4. Conclusions

Businesses operate in a dynamic, global and uncertain economic environment. This situation puts pressure on the finance function and its executive to better allocate resources and balance short term versus long term strategies, to counterbalance cost reductions with identifying long term growth opportunities. There are implications on the skills needed to face the challenges and this makes the career path in accounting and finance to evolve in new directions. It is both a challenge and an opportunity for the professionals looking for an enriching experience.

Challenges for the finance department are both in the human resource and in its infrastructure and technology. Human resource need to have additional skills in order to fulfill its role. Organizational structure becomes more complex with improved processes that incorporate technology in order to collect, analyze and report important financial data needed in the decision making process.

Synthesizing there are two main conclusions:

1. In what concerns the finance function transformation we can identify two key enablers: technology and people. The transformation of the finance function can be made more efficient and effective using the new technologies. But in order to use this technology at its value, a finance department has to have the right talents, with an appropriate mix of skills and knowledge.

2. In what concerns the role of the CFO there is an important shift and an upgrade from the traditional transactional role (reporting on the past) to a transformational, strategic role. The CFO has to undertake more value added and strategic activities.

The research on how financial managers and finance departments adapt to the changes in the environment will continue with a survey on CFOs in companies that operated in Romania, in order to test if the findings are applicable also to the Romanian market, or if we can identify some specificities in companies' approaches.

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