Gaining a Competitive Advantage: Critical Skills for CFOs and Controllers

GCA4/26/V1

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Course Outline

1. Introduction
2. Metrics and Benchmarking
3. Improving Efficiency
4. Artificial Intelligence
5. Bank Relationships and Cash Management
6. Risk Management
7. Economic Update

A Quick Word on Policy vs. Politics

- Many times when discussing accounting, tax and finance policy issues, it can be difficult to divorce the politics from the policy
- Today, when discussing the various issues we will encounter over the next several hours, let's agree to keep our own view of politics out of the application of the policy and focus on doing the very best we can for all our clients
- This goes for religious/faith views as well

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Chapter 1

Introduction

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Goals of the Program

- Goals of the program
  - Make you more valuable
  - Make your organization more valuable

Prepare To Be Frustrated

- This seminar is for decision makers
- You will learn and discuss the right way to do things
  - In some situations, you do not have the power to make change
    - That is frustrating

We Won't Cover All

- Far more material included in the materials than we can ever cover in a 4-hr. program
- Great reference materials to take home
- Speak up if you want to delve more deeply into any one area
  - Otherwise, we will go through with flexibility according to discussion

It’s All About Change

- Is your organization changing as fast as the world around it?
  - If not, it will fail or be bought out by another who is changing
- Changes in
  - Economy
  - Organizations
  - Society
  - Employees

According to Business Insider

- Finance professionals **MUST**
  - Become analytical wizards
  - Manage increasing risks
  - Adapt to new technology
  - Be better at leading people
  - Guide decisions in a politically charged atmosphere
  - Manage big data
  - Make effective decisions from data from outside the organization
  - Understand business drivers from outside the organization
  - Make better hiring decisions

Chapter 2

Metrics and Benchmarking

Learning Objectives

- Upon completing this chapter, the reader will be able to:
  - Understand the importance of using metrics as a way to manage for autonomy;
  - See how benchmarking and metrics go together for a management system;
  - Understand how to use the balanced scorecard; and
  - Know how to determine your key performance indicators

Problems To Avoid

- Data overload
- Politics

What Is the Objective of the Organization?

- How do you define success?
  - Crucial first step
  - Most organizations don’t do this
- How will you measure if you have reached success?
- Should be done by each department

KPI

- Longer term
- More strategic
- For upper management
- Harder to measure

Tactical Measurements

- Departmental level
- Immediate feedback
- Key is balance

Properties of Good Metrics

- Measure what is important
- Outputs more than inputs
- Measurable
- Controllable
- Simple and easy to explain
- Cost-effective to collect information
- Easy to maintain

Balanced Scorecard

- Strategic alignment
- Strategic performance
- Communications
  - Everyone should define “success” the same way

Four Perspectives

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Strategy

- Objective:
  - What do we want to accomplish?
- Measurement:
  - How will we measure to see if we are achieving?
- Target:
  - What is our target figure?
- Strategy:
  - How are we going to get there?

Levels

- Tier one:
  - Sr. management
- Tier two:
  - Divisional or departmental
- Tier three:
  - Individual or small team
- Always the same four perspectives

Who Determines the Metrics

- Old style:
  - The boss
- New style:
  - The individual or the team

ROWE and Metrics

- Results Only Work Environment
- Paying people and teams to do work and not put in time!

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Metrics for Financial Statements

- Current ratio
- Quick ratio
- Debt/Worth ratio
- Net profit/Net worth

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Causing Ratios

- Collection period
- Inventory turnover
- Fixed assets/net worth
- Sales/net worth
- Gross profit/sales
- Operating expenses/sales

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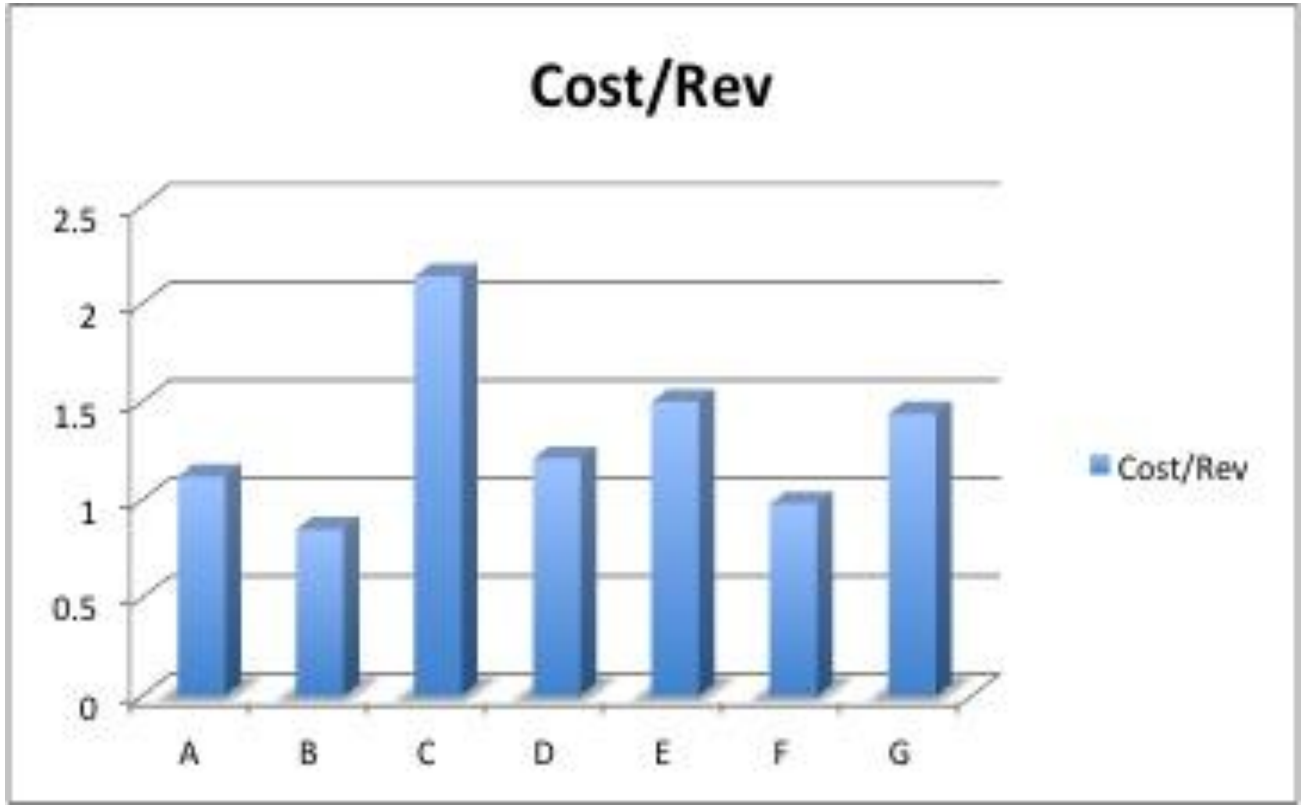
Benchmarking

- Internal:
  - Over time
  - Against other departments, divisions, etc.

External Benchmarking



External Benchmarking

- RMA:
  - Risk Management Associates
    - Industry averages
- Trade groups

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AI and Metrics

- From static reports to living metrics
- Smarter data collection: Beyond the general ledger
- New metrics emerge: From lagging to leading indicators
- Continuous forecasting and dynamic budgeting
- Decision support at the manager level
- AI turns financial metrics into a real-time feedback loop

Chapter 3

Improving Efficiency

Learning Objectives

- Upon completing this chapter, the reader will be able to:
  - Develop new ways to have a more efficient organization;
  - See better ways to delegate; and
  - Use ratios for better efficiency

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Only Two Things for Success

- Serve the customer well
- Do it efficiently

Two Ways To Increase Efficiency

- Old way:
  - Try to force employees to be efficient
    - Carrot and stick management; or
    - Taylorism – Trying to treat workers as machines
- New way:
  - Develop system where people want to be more efficient

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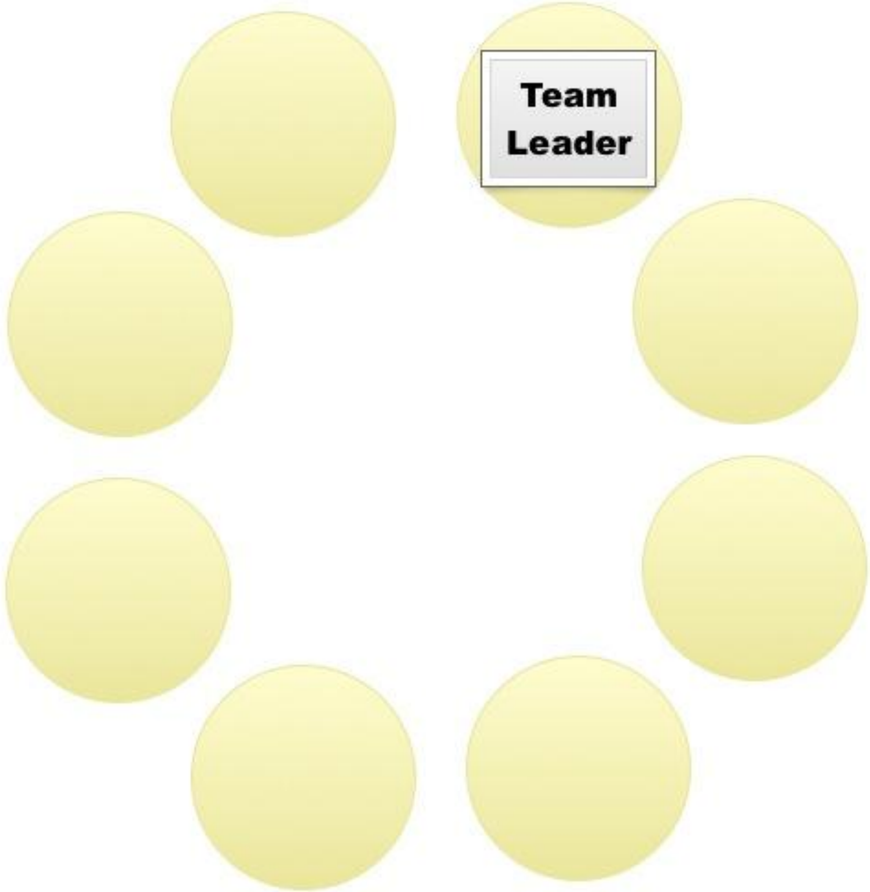
Cost of the Bureaucracy

New-Style Organization

Who Is the Smartest in the Room?



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Advantages of the Team-Style Organization

- Workers feel:
  - Trusted
  - Empowered
  - Engaged
  - More challenged
  - Valued

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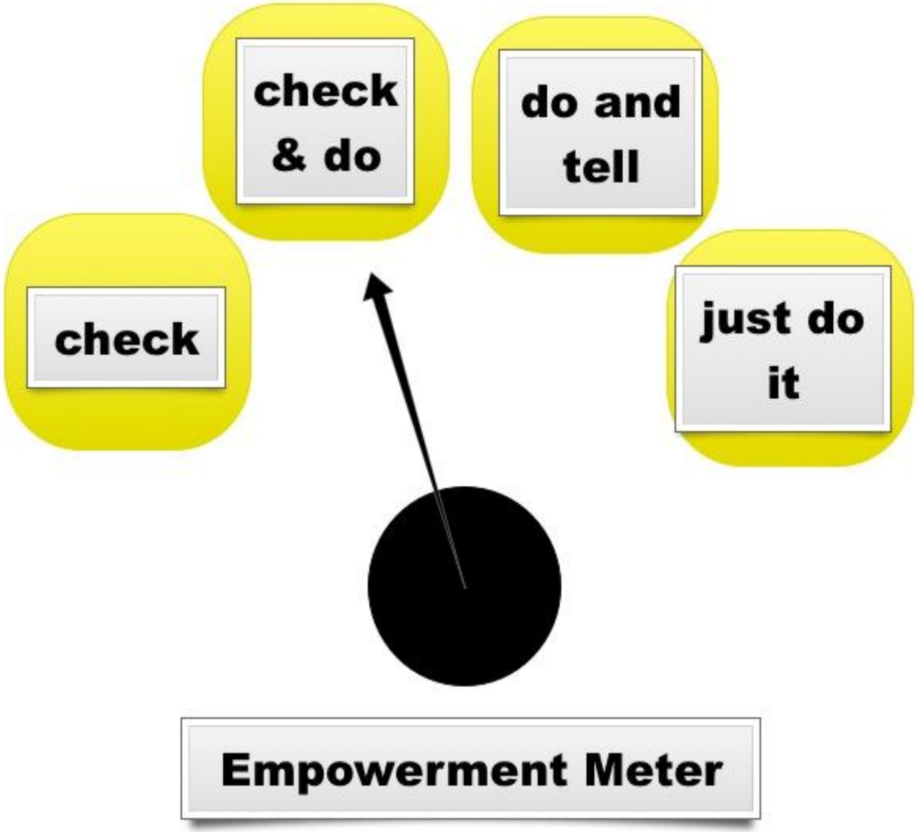
Empowerment Meter



Good Delegation

Responsibility

Authority

Accountability

Good Delegation

Productivity

- The relationship (ratio) between inputs and outputs
- Therefore, the key metric is to measure key relationships over time

Exercise

- Sam Brown is the recently named controller for the XYZ Services Company. This is a relatively small operation, and Sam is also the chief financial officer although he doesn't carry the title. The company has a sales force of 14 people who travel the country selling their products. In addition, several others of the executive team do some traveling
- One of the first assignments given to Sam was to increase the efficiency in the company. While it has always been profitable, the net profit margin has been slipping. As part of his analysis, Sam discovered that selling expenses as a percentage of sales has been increasing over the past five years as shown in the following graph

Metrics for Efficiency

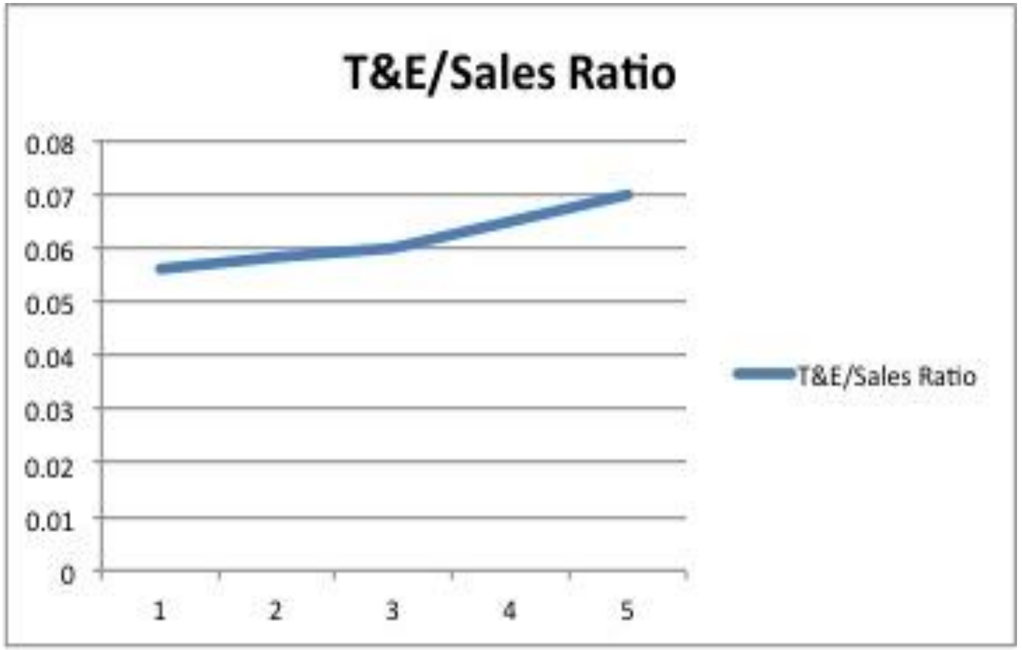
Exercise (Cont.)

- After a little more investigation, he discovered that travel and entertainment expenses accounted for almost a third of the selling expenses. Consequently, he determined that he should do something to try to increase the efficiency of the travel and entertainment expenses
- Review Sam's problem and make suggestions about what he might do

Ratios for Efficiency

- Peter Drucker
  - “Measure it and it will improve”
- You can improve almost anything
  - Numerator = the expense you want to improve
  - Denominator = cost driver
- Example: T&E to Sales

T&E/Sales Ratio



T&E/Sales Ratio

- Company
- Division
- Department
- Individual salesperson

Other Expense Ratios

- Occupancy costs – occupancy costs/sales
- Utilities – utility expenses/head count
- Transportation expenses – transportation expense/sales
- Auto expenses – auto expense/sales or auto expense/head count
- Consulting services – consulting services/sales
- Advertising – advertising expenses/sales
- Marketing – marketing expenses/sales
- Bad debts – write offs/sales, write offs/receivables, or past due/either sales or receivables
- Dues and publications – dues and publications/head count
- Office supplies – office supplies/head count
- Salaries and wages – salaries and wages/sales or head count
- Fringe benefits – fringe benefits/salaries
- Telephone – telephone expenses/head count

Exercise

- Consider an expense you believe could be better controlled
- What ratio might you develop to monitor for improvement

Ratios To Prevent Fraud

- Develop ratios that will show if an expense is out of line
- Benchmark that ratio over like groups
- Look for potential problems

Exercise

Jim is controller of Last Manufacturing Company. Recently his boss has told him that the company has a new bank relationship that requires a faster and more recent close with more details being provided to the bank. Jim knows that this will require more work by the accounting department and must decide how the additional work will be allocated.

In this situation, how would you go about determining who should get the additional work?

A similar kind of question often comes up when determining who to hire either to replace a person in the department or add to the staff level. In the bureaucratic organization, that decision would be made solely by the department head. In the team-centered organization, the decision would be made by the department head, but only after a lot of discussion with the team.

AI and Efficiency

- Automating repetitive tasks
- Improving decision-making with data
- Enhancing customer support
- Optimizing operations and resources
- Scaling without proportional cost increases

Chapter 4

Artificial Intelligence

Learning Objectives

- Upon completing this chapter, the reader will be able to:
  - Review the benefits of AI in finance and where AI is already used;
  - Identify risks related to internal control, data integrity, and cybersecurity; and
  - Understand the regulatory landscape relating to AI

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Artificial Intelligence in Corporate Finance Leadership, Governance, and Responsibility

- AI is rapidly transforming finance functions
- Creates major opportunities and serious risks
- CFOs and controllers face a defining leadership challenge
- Core theme: **AI can assist judgment – not replace responsibility**

Why AI Is a Strategic Finance Issue

- Every generation of finance leaders faces major change
- AI differs from prior technology:
  - Generates explanations and predictions
  - Communicates in natural language
  - Influences decisions
- Boards now expect finance leaders to explain:
  - AI usage in forecasting
  - Reliability of outputs
  - Compliance with controls and regulations

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The Governance Challenge

- AI is moving faster than policies and controls
- Risk of:
  - Blind spots in internal control
  - Weak documentation
  - Reduced accountability
- Avoiding AI → lost productivity
- Blind adoption → loss of oversight
- Finance leadership must guide adoption

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How AI Differs From Traditional Systems

- **Deterministic vs. probabilistic thinking**
- Traditional systems:
  - Rule-based
  - Produce fixed outputs
- AI systems:
  - Probability-based
  - Generate likely – but not certain – results
  - Can produce plausible but incorrect conclusions
- Key concept:
  - **Confidence ≠ accuracy**

Human Risk: Over-Trusting AI

- People tend to trust AI because it appears sophisticated
- Risk of "rubber-stamping" outputs
- AI may:
  - Fabricate references
  - Miss causal relationships
  - Reflect hidden assumptions
- Finance teams must be trained to:
  - Challenge AI
  - Verify assumptions
  - Maintain skepticism

Where AI Is Already Used in Finance

- **Operations**
  - Detect unusual journal entries
  - Suggest accruals
  - Draft narratives
- **Forecasting and modeling**
  - Rolling forecasts
  - Scenario simulations
  - Variance analysis
- Opportunity
  - Faster processes
  - Broader data analysis
- Risk
  - Hidden logic
  - Weakened review processes

Strategic Benefits of AI

- AI enables:
  - Review of 100 percent of transactions
  - Faster close cycles
  - Early detection of control failures
  - Faster executive reporting
- Talent impact:
  - Less routine work
  - More focus on:
    - Interpretation
    - Risk assessment
    - Strategic insight

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Major Risks CFOs Cannot Ignore

- **Internal control risk**
  - AI operating outside documented controls
  - Difficult to audit outputs
- **Data integrity risk**
  - Poor inputs → flawed insights at scale
- **Cybersecurity risk**
  - Confidential data exposure
  - Vendor and regulatory risks

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Accountability, Ethics, and Regulation

- AI does not assume liability – humans do
- Ethical leadership requires:
  - Clear ownership
  - Documented review
  - Avoiding blind reliance
- Regulators expect:
  - Effective controls
  - Transparent documentation
  - Human accountability
- SOX and audit standards still apply

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The Future Role of Finance Leadership

- **AI governance framework**
  - Approved use cases
  - Mandatory human review
  - Clear documentation
  - Continuous monitoring
- Implementation steps:
  1. Inventory AI usage
  2. Pilot low-risk opportunities
  3. Establish governance
  4. Train teams
  5. Engage audit committees
- Final message:
  - **AI will amplify finance – leadership will determine whether it strengthens or weakens trust**

Chapter 5

Bank Relationships and Cash Management

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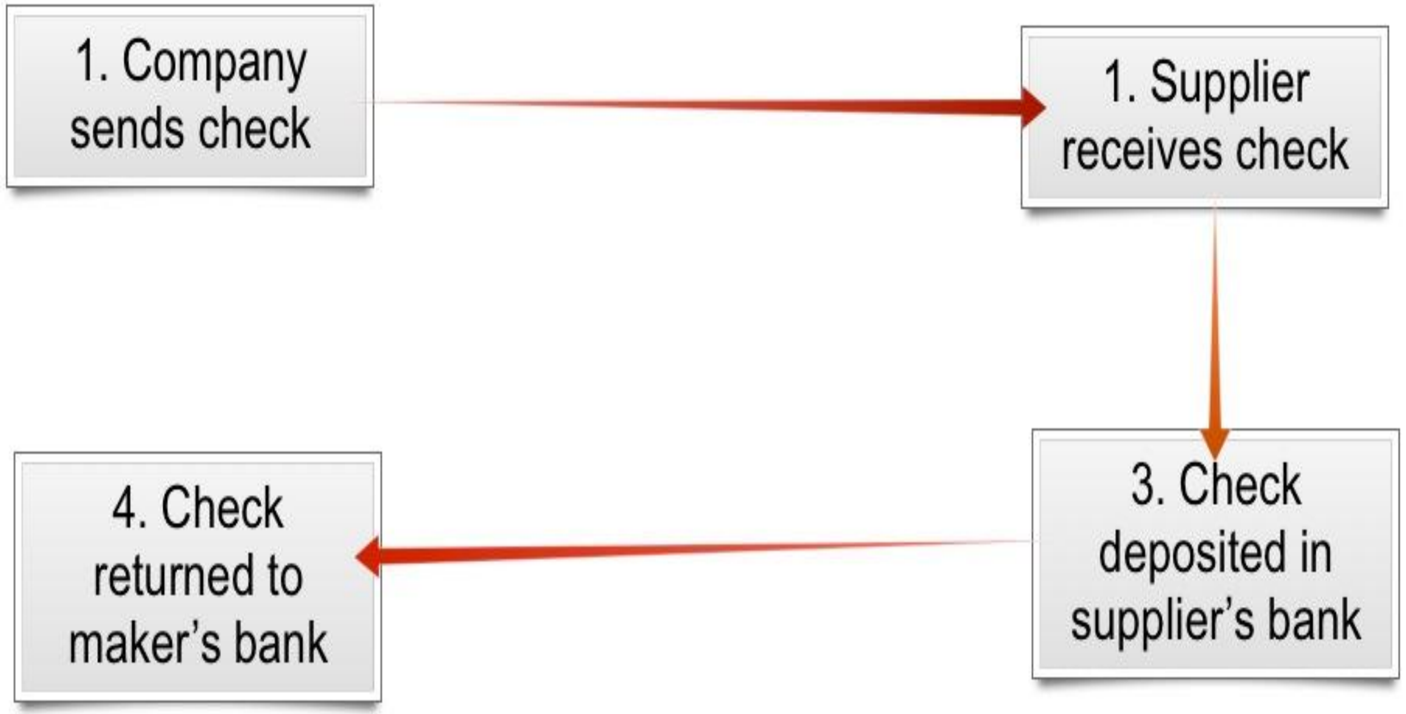
Learning Objectives

- Upon completing this chapter, the reader will be able to:
  - Better understand modern cash management;
  - Understand how to negotiate with a bank for a loan; and
  - See some of the consequences of modern banking laws

Check Clearing



Check 21

- Allow digitizing checks for clearing

Dodd-Frank Legislation

- Compliance costs
- Interest on deposits
- Tighter credit standards

Modern Cash Management

- No longer about float management
  - Little float
  - Relatively low interest rates
- Now about efficiency
  - Automatic payments and receipts
  - Treasury systems
  - Computerization
- The answer is to ask the banks what is available

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AI With Cash Flow and Banking

- From reactive to predictive cash control
- Real-time cash visibility
- Smarter working capital optimization
- Automated cash forecast adjustments
- Enhanced risk detection and fraud prevention
- Strategic role of finance teams

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Bank Borrowing

- (L * R * U) + (L * F) / (L * U) – (C + (L*F)

- B = Average line balance
- R = Interest rate charged
- U = Usage of line
- L = Amount of line of credit
- F = Fee being charged online
- C = Compensating balances kept at bank

Example

- Customer view

Line	1,000,000
Rate	5%
Balances	150,000
Fee	1%
Usage	40%
Fees and interest paid	30,000
Net funds received	240,000
Yield	12.50%

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Example (Cont.)

- Bank view

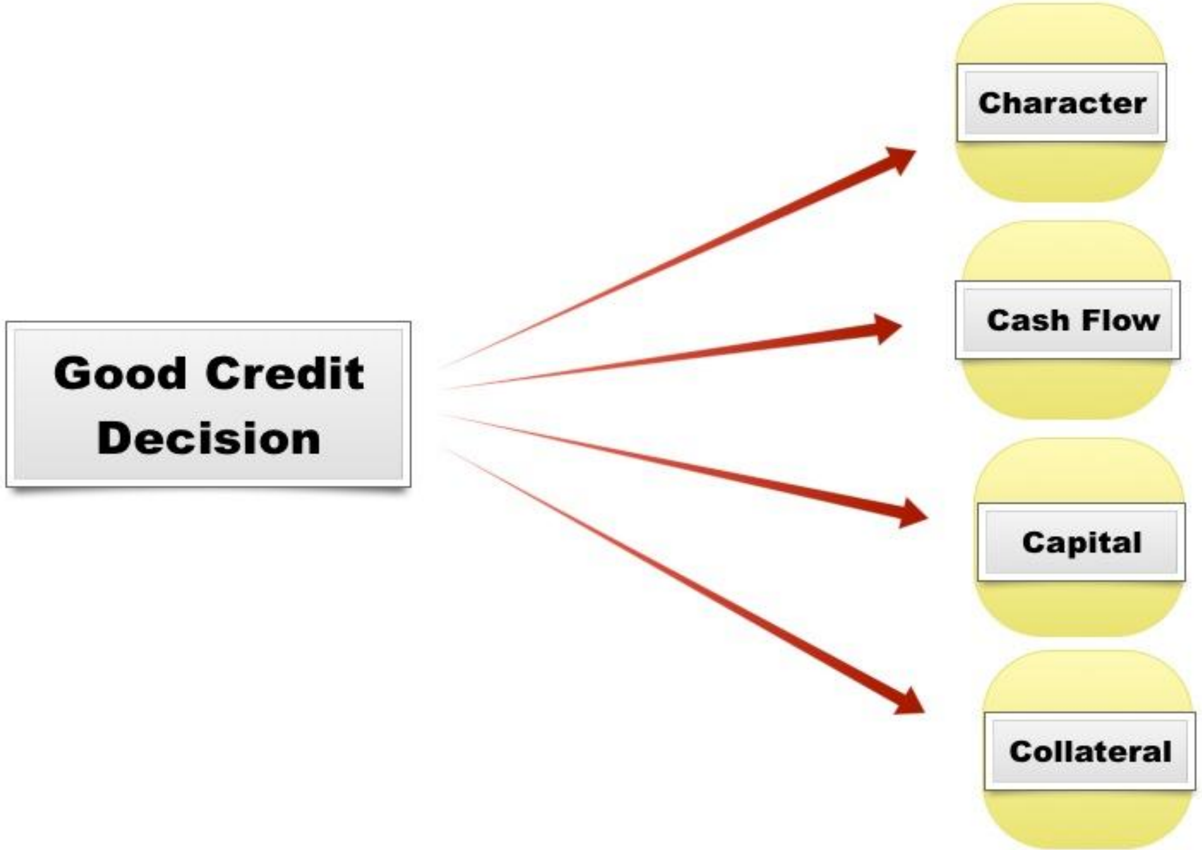
Line	1,000,000
Rate	5%
Balances	150,000
Fee	1%
Usage	100%
Fees and interest paid	60,000
Net funds received	840,000
Yield	7.14%

Win/Win Solution

Line	1,000,000
Rate	6.00%
Balances	150,000
Fee	0.50%
Usage	40%
Fees and interest paid	29,000
Net funds received	245,000
Yield	11.84%

Line	1,000,000
Rate	6.00%
Balances	150,000
Fee	0.50%
Usage	100%
Fees and interest paid	65,000
Net funds received	845,000
Yield	7.69%

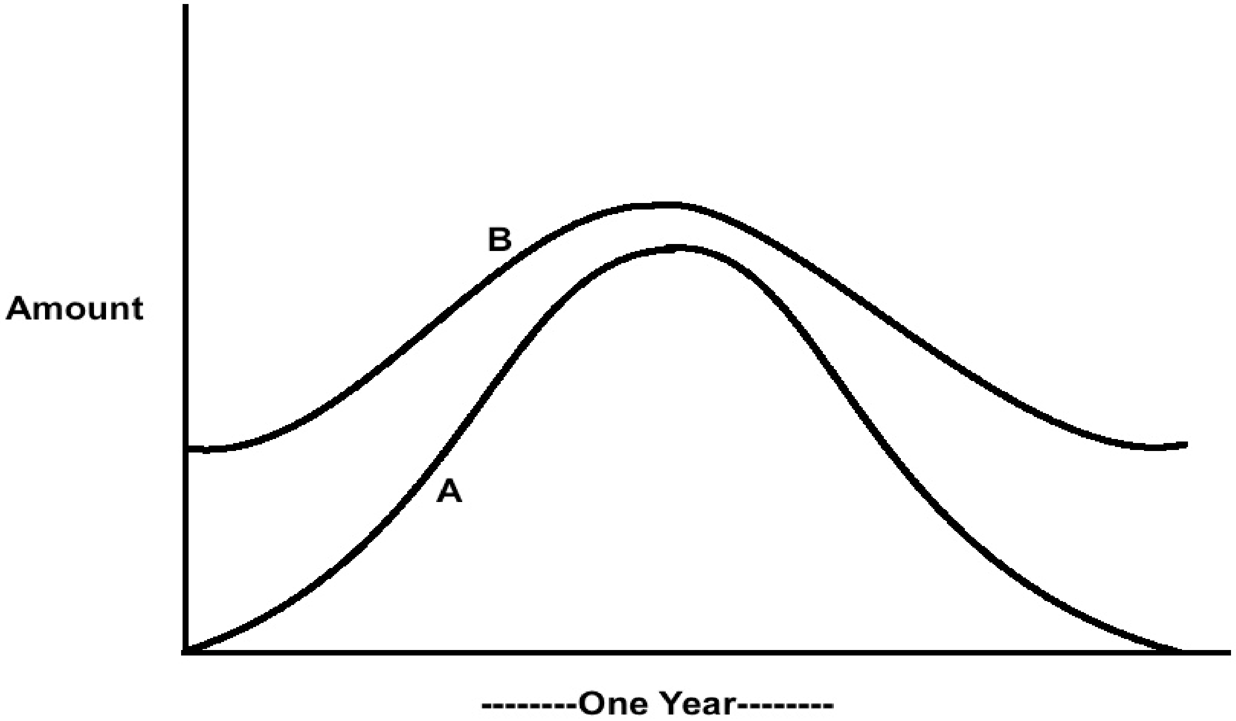
The Four Cs of Credit



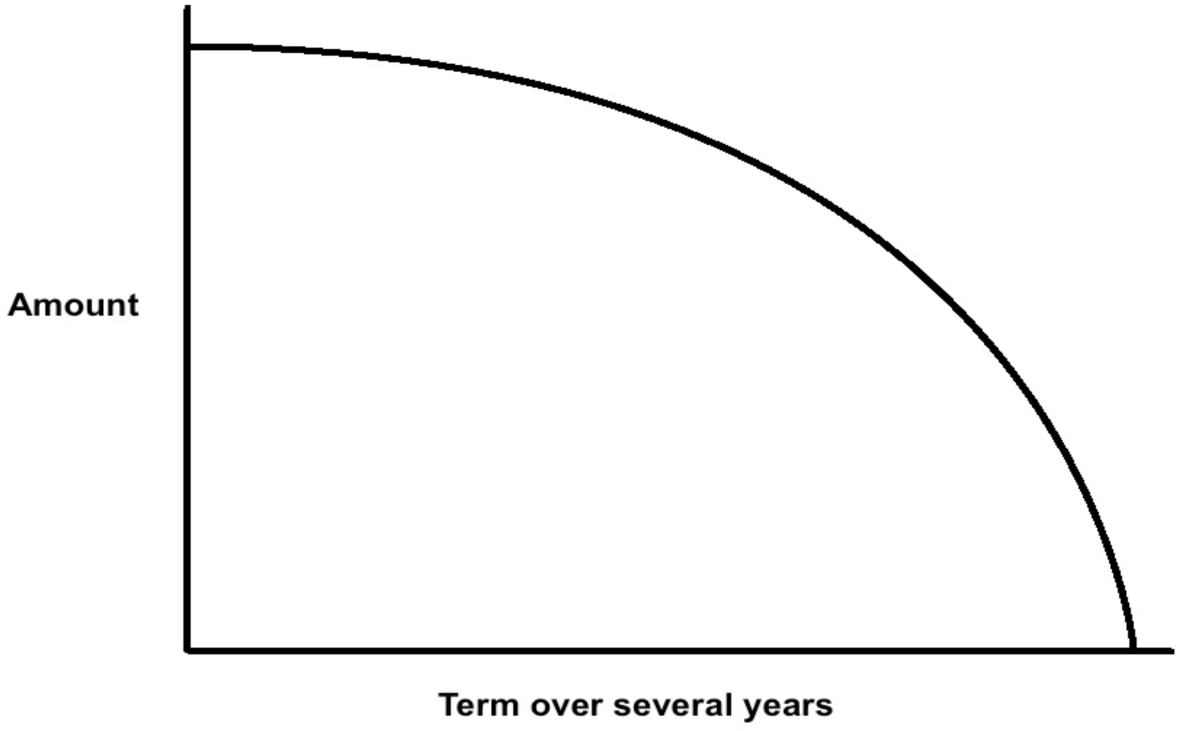
Character

- History
- Rating agencies and D&B:
  - Public records
  - Trade payment information
  - Financial information
  - Financial analysis
  - Strategy
- Personal credit reports
- Bank references

Cash Flow – Short Term



Cash Flow – Long Term



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Cash Flow Ratios

- Current
- Quick
- Cash flow (after profit + depreciation) / current portion of LTD

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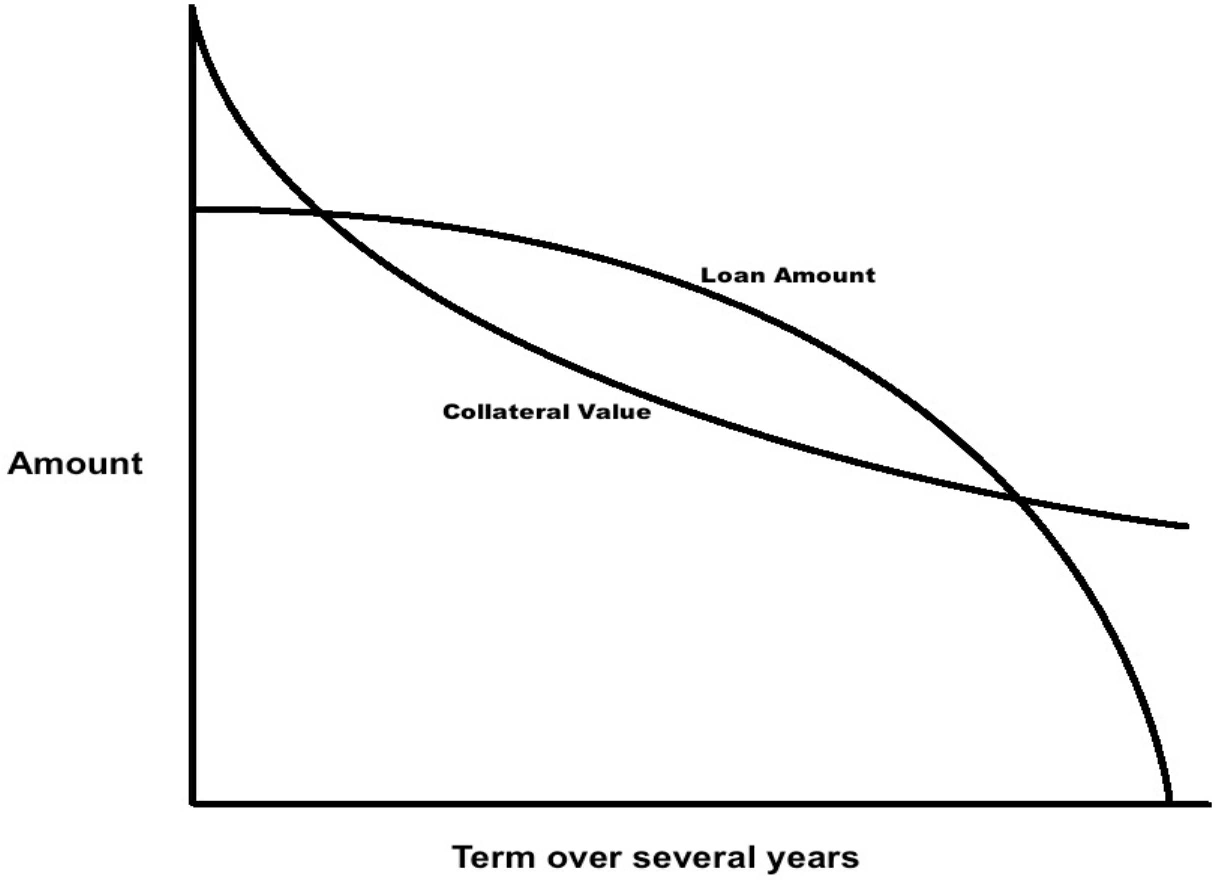
Capital

- Total debt / net worth
- Total debt / total assets

Collateral



Loan Amount
Collateral Value
Amount
Term over several years

Simple But Effective System

<u>Character</u>	<u>7</u>
Cash Flow	7
Capital	7
Collateral	7

- Rule: You must have the first C, then you must have two of the second group

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AI and Bank Borrowing

- Faster loan decisions
- Smarter credit risk assessment
- More accurate risk pricing
- Reduction in human bias through standardized decision models
- More customized loan products
- Dynamic loan terms based on actual business performance
- Ongoing monitoring instead of one-time underwriting

Chapter 6

Risk Management

Learning Objectives

- Upon completing this chapter, the reader will be able to:
  - Recognize organizational risks often not detected;
  - See how to establish an ERM system;
  - Determine how to respond to known risks; and
  - See how to determine unknown risks

ERM

- Identify relevant events, developments, and circumstances
- Classify into likelihood of magnitude and impact
- Develop strategy to mitigate or seize opportunity
- Monitor the organization toward these objectives

Companies Who Missed the Upside

- Wal-Mart
- Digital Equipment
- Wang Laboratories
- Research in Motion
- Smith Corona
- Kodak

Key Point

- If your organization isn't changing as fast as the environment, you have a problem

Why We Don't Change

- Size of organization
- Type of organization
- Incentives and risk
  - More employee ownership = more willingness for risk
- Effects of current recession

Behavioral Economics and Risk

- Conformity
- Obedience
- Ambiguity aversion
- Representativeness
- Optimism

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What Is Your Willingness to Take Risk?

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Risk and the Business Model

- For many, our greatest and often not discussed risks:
  - Education
  - Government
  - Disintermediation
  - Internet

Risk of Disruptive Innovation

- Disintermediation
- Artificial intelligence (AI)
- Blockchain
- 3D printing

Economics and Risk

- Is what we are doing sustainable?
- Watch indicators compared to benchmarks

Discussion Question

- What things in the economy might affect your business model?

Risk and Strategic Planning

- Are we all on the same page?
  - Vision
  - Mission
  - Core values
- Are we planning for the future?
  - Change of administration

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Risk Owners

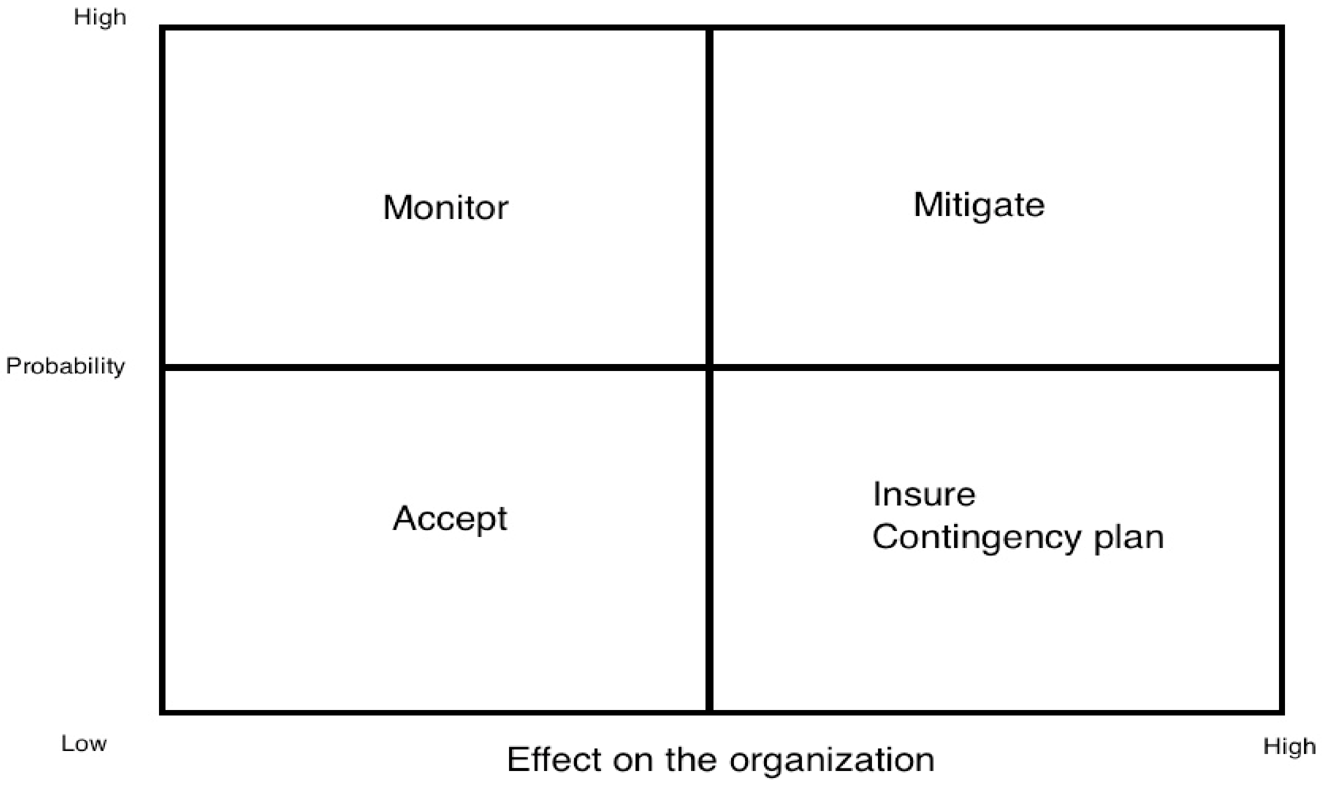
- One person has to accept the responsibility
- Monitor centrally
- Manage decentrally

Risk Categories

- Production
- Marketing
- Cash flow
- Compliance
- Business disruption
- Reputation

Manage Known Risk

Risk Management Plan



Final Questions

- What's the worst that can happen?
- What's the upside?
- What are the probabilities?
- What are the potential positive and negative effects?
- How will we mitigate and manage?

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Accounting Risk

- Going concern
- Cost basis of accounting
- Accrual basis of revenue
- Current assets
- Fixed assets
- Intangible assets
- Current liabilities
- Long-term debt

Cash Flow Risk

- $EFN = SA/S * \Delta S + \Delta FA - SL/S * \Delta S - (S + \Delta S) * PM * (1 - PO)$

- SA – Spontaneous assets. These are assets that automatically grow with sales growth, and usually consist of cash, receivables, and inventory
- S – Sales
- SL – Spontaneous liabilities. These are liabilities that automatically grow with sales growth, and usually consist of payables and accruals
- FA – Fixed assets
- PM – Profit margin (net of taxes)
- PO – Payout ratio

Cash Flow Risk

Cash	10,000
Accounts Receivable	120,000
Inventory	150,000
Fixed Assets	210,000
Accounts payable	100,000
Accruals	45,000
Sales	800,000
Net profit	50,000
Dividends	30,000
Spontaneous assets	280,000
Spontaneous liabilities	145,000
Profit margin	0.06250
Payout ratio	0.60000
Assumptions:	
New sales	-
New net fixed assets	-

Spontaneous assets/sales	0.350000
Spontaneous liabilities/sales	0.181250
Spontaneous assets increase	-
Spontaneous liabilities increase	-
Net fixed assets increase	-
New sales	800,000
Profit	50,000
Dividends	30,000
Net change in cash flow	20,000

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Cash Flow Risk

Cash	10,000
Accounts Receivable	120,000
Inventory	150,000
Fixed Assets	210,000
Accounts payable	100,000
Accruals	45,000
Sales	800,000
Net profit	50,000
Dividends	30,000
Spontaneous assets	280,000
Spontaneous liabilities	145,000
Profit margin	0.06250
Payout ratio	0.60000
Assumptions:	
New sales	80,000
New net fixed assets	-

Spontaneous assets/sales	0.350000
Spontaneous liabilities/sales	0.181250
Spontaneous assets increase	28,000
Spontaneous liabilities increase	14,500
Net fixed assets increase	-
New sales	880,000
Profit	55,000
Dividends	33,000
Net change in cash flow	8,500

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Cash Flow Risk

Cash	10,000		
Accounts Receivable	120,000		
Inventory	150,000		
Fixed Assets	210,000		
Accounts payable	100,000		
Accruals	45,000		
Sales	800,000		
Net profit	50,000		
Dividends	30,000	Spontaneous assets/sales	0.350000
		Spontaneous liabilities/sales	0.181250
Spontaneous assets	280,000		
Spontaneous liabilities	145,000	Spontaneous assets increase	28,000
Profit margin	0.06250	Spontaneous liabilities increase	14,500
Payout ratio	0.60000	Net fixed assets increase	10,000
		New sales	880,000
Assumptions:		Profit	55,000
New sales	80,000	Dividends	33,000
New net fixed assets	10,000		
		Net change in cash flow	(1,500)

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Cash Flow Risk

Cash	10,000		
Accounts Receivable	120,000		
Inventory	150,000		
Fixed Assets	210,000		
Accounts payable	100,000		
Accruals	45,000		
Sales	800,000		
Net profit	50,000		
Dividends	30,000	Spontaneous assets/sales	0.350000
		Spontaneous liabilities/sales	0.181250
Spontaneous assets	280,000		
Spontaneous liabilities	145,000	Spontaneous assets increase	56,000
Profit margin	0.06250	Spontaneous liabilities increase	29,000
Payout ratio	0.60000	Net fixed assets increase	50,000
		New sales	960,000
Assumptions:		Profit	60,000
New sales	160,000	Dividends	36,000
New net fixed assets	50,000		
		Net change in cash flow	(53,000)

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Issues To Be Corrected

- Cash management
- Accounts receivable turnover
- Inventory turnover
- Fixed assets
- Gross margin
- Operating expenses
- Dividend policy

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Financial Leverage

	Company A	Company B
Cash	10,000	10,000
Receivables	126,000	126,000
Inventory	175,000	175,000
Current assets	311,000	311,000
Fixed assets	100,000	100,000
Total assets	411,000	411,000
Bank debt	-	50,000
Payables	105,000	105,000
Accruals	15,000	15,000
Current liabilities	120,000	170,000
Long term debt	-	150,000
Total liabilities	120,000	320,000
Common stock	191,000	50,000
Retained earnings	100,000	41,000
Total equity	291,000	91,000
Total liabilities and equity	411,000	411,000
EBIT margin	6.00%	6.00%
Interest rate	9.00%	9.00%
Sales	1,000,000	1,000,000
EBIT	60,000	60,000
Interest rate	-	18,000
Net earnings before taxes	60,000	42,000
Taxes (30%)	18,000	12,600
Net earnings after taxes	42,000	29,400
Return on equity	14.4%	32.3%
Debt/worth	0.41	3.52

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Operating Leverage

	Company A (hotel)	Company B (grocery store)
Sales	10,000,000	10,000,000
Variable expenses	1,500,000	7,500,000
Marginal contribution	8,500,000	2,500,000
Fixed costs	7,500,000	1,500,000
Operating profit	1,000,000	1,000,000

Profits with a 20% increase in sales

	Company A (hotel)	Company B (grocery store)
Sales	12,000,000	12,000,000
Variable expenses	1,800,000	9,000,000
Marginal contribution	10,200,000	3,000,000
Fixed costs	7,500,000	1,500,000
Operating profit	2,700,000	1,500,000

AI and Risk Management

- Shift from periodic reviews to continuous risk monitoring
- Move from reactive to predictive risk management by identifying patterns and early warning signs
- Enhance financial risk detection through continuous monitoring of cash flow, expenses, and receivables
- Identify liquidity problems and fraud at earlier stages
- Strengthen cybersecurity and operational risk control
- Detect cyberattacks and data breaches through AI-driven threat analysis
- Monitor network behavior and access patterns in real time

AI and Risk Management

- Improve supply chain and vendor risk management
- Diversify suppliers or renegotiate contracts before problems escalate
- Simplify compliance and regulatory risk management
- Automate the monitoring of transactions and documentation
- Generate alerts for policy violations and regulatory changes
- Integrate risk insights into everyday business tools
- Replace complex risk reports with clear, actionable dashboards

Chapter 7

Economic Update

Learning Objectives

- Upon completing this chapter, the reader will be able to:
  - Recognize key emerging economic trends;
  - See how micro and macroeconomics work together;
  - Understand how new things like the cloud and social media affect our organizations; and
  - Better predict what may happen to our business

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Why Economics Is Important To You

- You are the numbers person therefore
- You are the company economist

Microeconomics

Key Economic Trends

- Globalization
- Industrial to knowledge economy
- The connected economy
- Non-employee employees
- Retail to the Web
- Technology to the cloud

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Microeconomics and Trends

- Elements of production changing:
  - We need creative people
- Spoiled customers
- Hyper competition

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Disintermediation

- Cutting out the middleman
- Examples
  - Manufacturer directly to the customer
  - Online education
- Internet if usually the vehicle used

The AI Economy

- Productivity has increased
- Labor markets are being rewired
- Markets are becoming more efficient
- Firm structure is changing
- Inequality pressures have increased
- Changes in economics itself
- Policy debates

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Exercise

- How might disintermediation affect your organization?
- Are there any ways that you can become the one doing the disintermediation?

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Exercise

- What trends can/will affect your organization?

Macroeconomics

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Money Supply

- Must remain in balance to growth in GDP
  - Too much money = inflation
  - Too little money = lack of growth

- Definition of money
  - Medium of exchange or store of value
  - For regulatory purposes
    - Cash and currency + demand deposits in commercial banks

How Is Money Created?

- Government spends more than it takes in
  - Deficit spending
- Banking system
  - When a loan is made, money supply increases
  - When a loan is repaid, money supply declines

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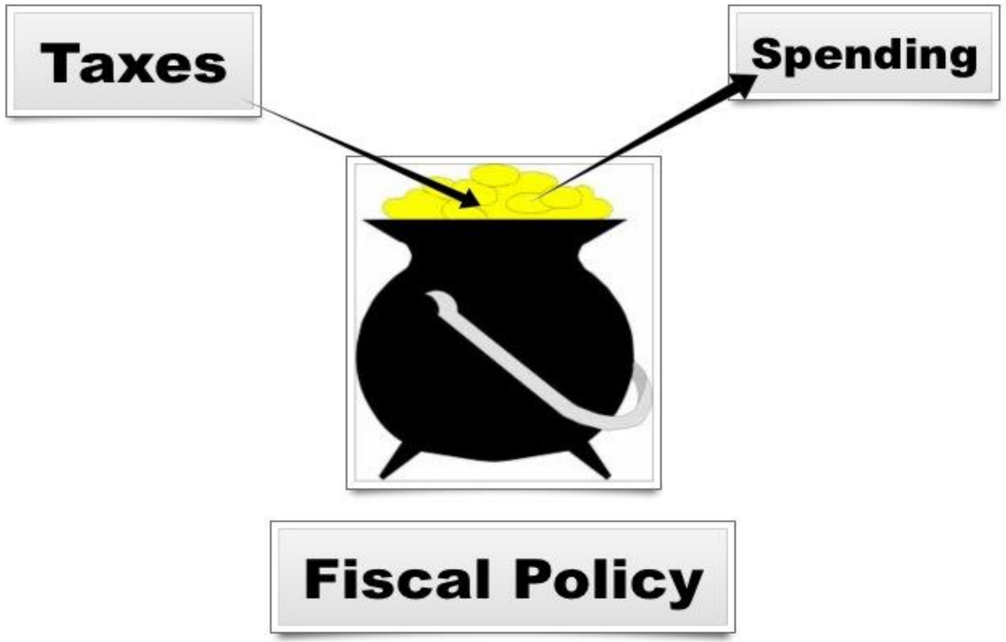
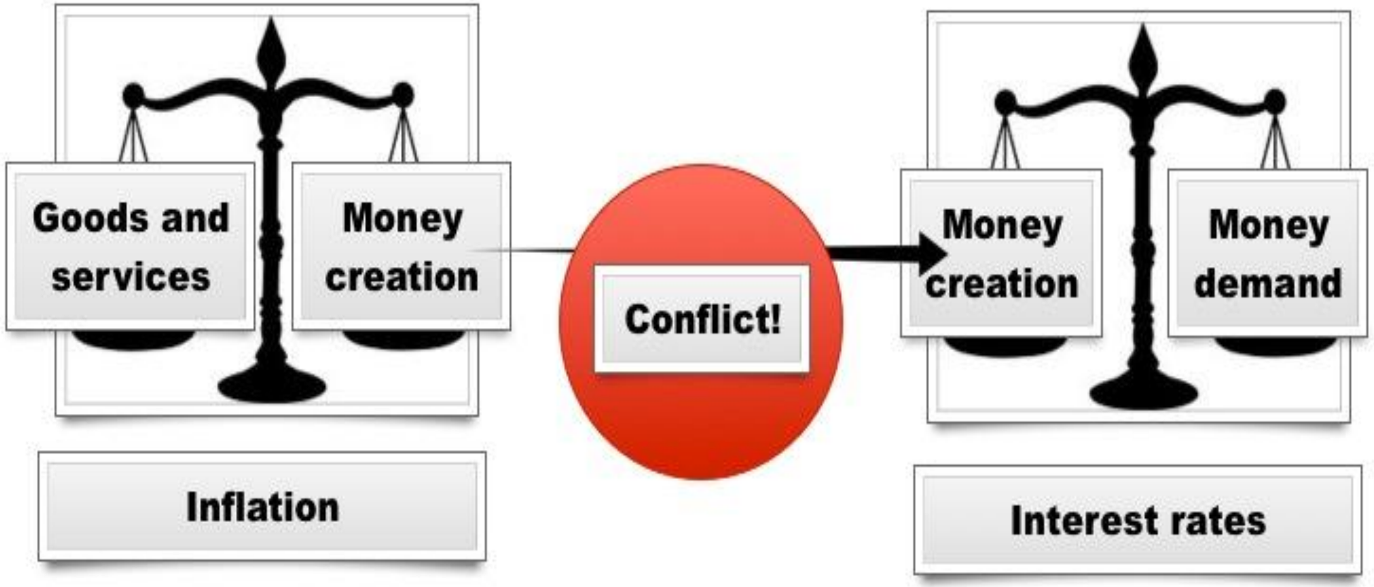
Fiscal Policy



Monetary Policy

- Controlling the amount of new money that the banks can create
  - Discount rate
    - Fed funds rate
  - Reserve requirements
  - Open market operations

Monetary Policy



What's Happening Now

- Prior to pandemic, things in balance
- Pandemic
  - Government closed much of the economy
  - A lot of deficit spending to offset
    - Probably went too far
- Fiscal policy allowed money supply to grow too fast
  - Inflation resulted
- Fed increasing interest rates to try and bring down money supply growth
  - Conflict between monetary and fiscal policy

Economic Predictions

- Views of many economists as well as the author

- Economic growth
  - Some indicators up, others down
  - Prediction is continued slowing of GDP and housing
    - Probably continuing into employment
  - Fed is hoping for a "soft landing," may pull it off
- Interest rates
  - Continue up a little more and then drop as economy falters

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Thank you!