The 6 Secrets of a successful CFO - Part II

Achieving financial success for your company

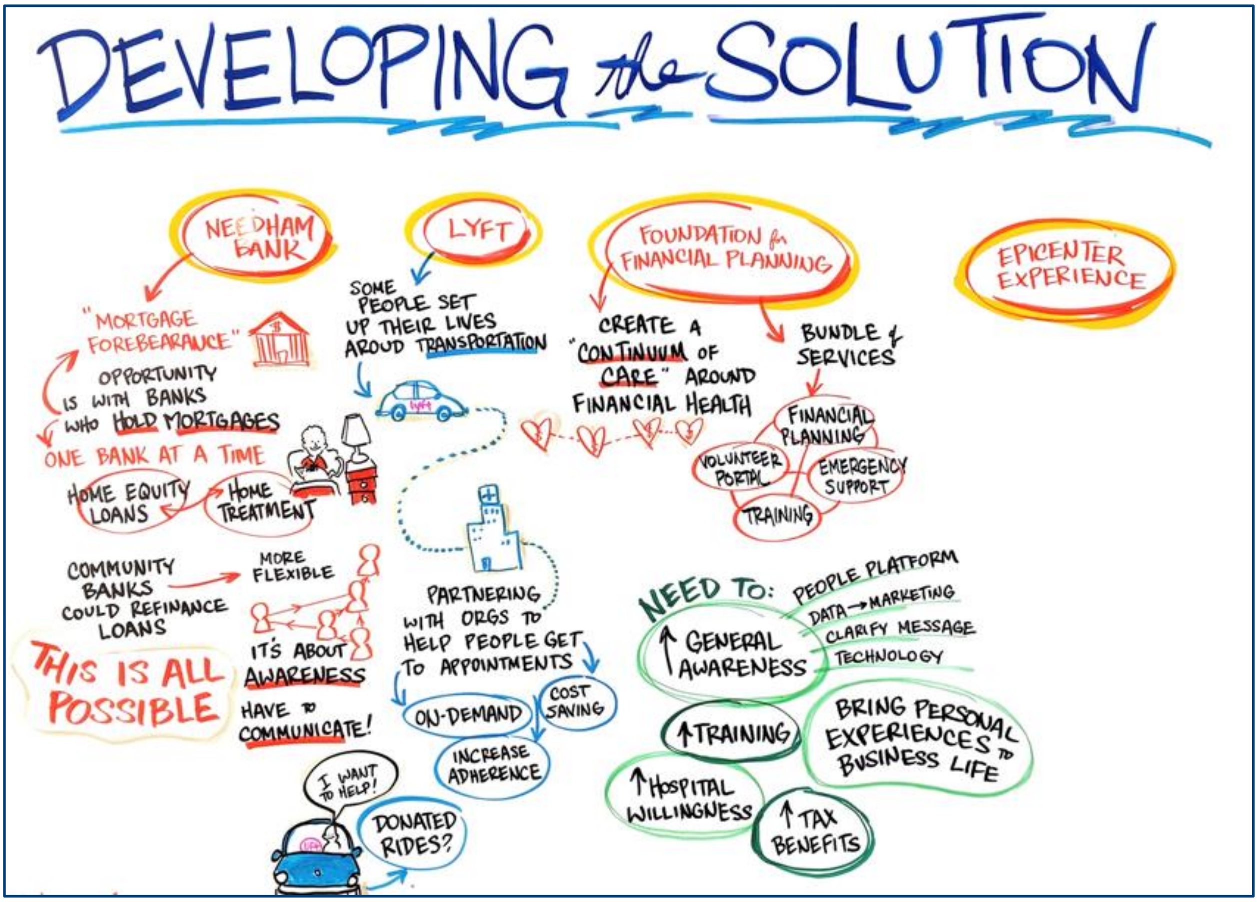
FOREWORD

This is the second part of something which does not aim to be an academic manual (this being an area already covered by top-flight writers). Instead, it sets out to highlight the types of behaviour that Clarkson Hyde Professionals come across most frequently in the companies they work with, whilst highlighting simple factors which, if successfully harnessed, can prove particularly valuable for companies, without requiring major effort.

In this edition of Food for Thought, we will look at the second three secrets of a successful CFO.
Along with the first part sent out last month we hope you find these insights useful.

In the first part we talked about the first three secrets such as:

1. **SECRET 1:** TRY TO LEARN WHERE YOU ARE EARNING AND WHERE YOU ARE LOSING OUT!
2. **SECRET 2:** PREPARE A CASH FLOW PLAN!
3. **SECRET 3:** BE CAREFUL WITH INVESTMENT IN WORKING CAPITAL!



SECRET 4
FIND OUT ABOUT ALL THE FINANCIAL INSTRUMENTS ON THE MARKET!

All too often, companies only have one provider to cover their financial needs: the bank. And perhaps only one bank at that, because it is convenient and close by!

But the market is constantly evolving, and each day it brings out new products to fund credit-worthy businesses, often at costs that are lower than those offered by the banks themselves.

From the standpoint of **debt capital**[1] for example, the latest innovations are minibonds and financing bills.

Minibonds are a financing instrument (bonds issued within a clearly-defined regulatory framework which has now become a consolidated practice) which can allow small and medium-sized businesses to fund their growth projects through a channel which offers an alternative to the banking systems; **financing bills,** on the other hand, are promissory notes.

To all intents and purposes, they act as a collection of savings from the public, using a collective funding instrument.

From the standpoint of **risk capital**[2], however, venture capital companies[3], private equity funds[4] or the AIM segment of the Stock Exchange for SMEs[5] can provide interesting solutions for companies whose books are in order.

Then there is the subject of **subsidised loans**, which can provide help in less favourable economic periods, including with non-refundable grants which do not need to be repaid, or other loans with a subsidised rate and a capital cost which is consequently lower.

In order to obtain the widest possible resources at a lower cost, the company may request access to the **guarantee fund** if any in the respective Country**.** This is aimed at small and medium-sized businesses and professionals from every sector, for any financial operation involved in their entrepreneurial activities.

In addition, the State's guarantee allows banks to grant loans (even on a long-term basis) at costs that are lower for the company.

Each of these topics would in itself be worth dedicating a book to, but experienced professionals are needed to help companies understand what approaches they can pursue when in search of capital for their businesses.

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[1] Debt capital involves funds that companies receive from third parties (first and foremost banks, financial institutions, providers or even employees, on occasion) whether on a payment basis or otherwise, but which they must in any case return within a given, variable period of time.

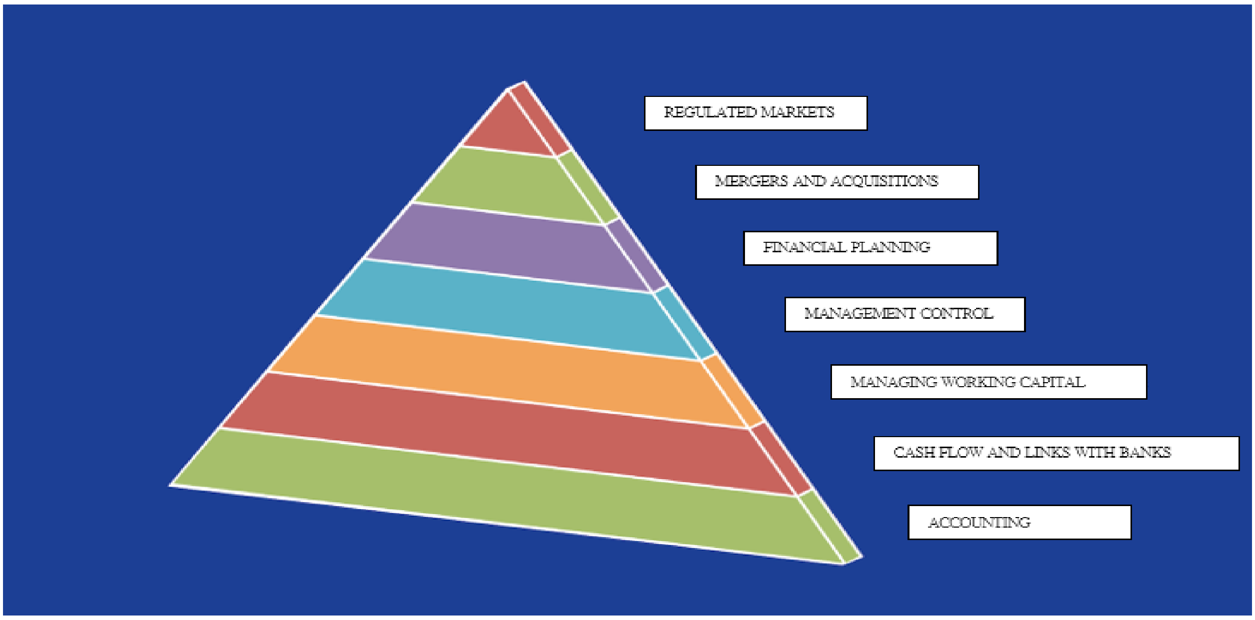
[2] The risk capital is that which is supplied by the owner (in the case of an individual company) or partners (in the case of companies) and there is no fixed date for its repayment.

[3] Venture capital companies or funds supply risk capital to finance the set-up or growth of a business in sectors that have high development potential, such as digital technologies.

[4] Private equity companies or funds invest in risk capital to support the growth of companies not floated on the stock exchange. Unlike venture capital, they mainly invest in larger-size companies operating in traditional sectors.

[5] AIM or Alternative Investment Market is the market segment of the Stock Exchange dedicated to SMEs, small and medium enterprises.

SECRET 5
MAKE YOUR COMPANY GROW ON THE FINANCE PYRAMID!



When I go into companies, I tell the managers and my co-workers about what I call the "**Pyramid of Finance**"[6] which shows all the activities involved in the financial area ordered from the bottom upwards, based on their potential for creating value for shareholders.
I have noticed that it is always something that arouses considerable interest, which proves that the financial culture in Italian companies has considerable room for improvement.
All companies have the first two steps to some extent or other, not least in order to meet regulatory and legal requirements (accounting) as well as basic operational needs (every company has at least one current bank account); as we work our way up the pyramid, the degree of complexity of the business increases, regulatory restrictions tend to reduce considerably, and only a handful of companies reach the function at the top of the pyramid.
Nonetheless, it is the activities located highest up that have the greatest impact on how the company is managed. Yet whilst they might be useful or even necessary, often they are overlooked, or they are handled by people without the skills required for the task.
For example, many of the companies I have come across, at times even large ones, tend to delegate management of the financial area to the accounts office. Often they fail to grasp that **accounts and finance are two departments** which are complementary, but **different**.
Accountants are traditionally people geared towards internal affairs, reporting and compliance[7]. Finance has an external outlook and therefore calls for communication, analytical and strategic vision skills. Accounting has to reason "ex post", whilst finance has to use an "ex ante" approach.
Accountants have the crucial task of producing a correct and truthful representation of the company. The role of finance managers, on the other hand, requires greater skills when it comes to qualities needed to provide strategic support to administrators and managers: they are specialists who have to **monitor** key parameters such as cash flow, **striking the balance between the company's own resources and loan capital, and generating value.**

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[6] The term Finance Department in Anglo-Saxon companies usually refers to the administration, finance and control area.
[7] The term compliance refers to controlling that ensures the company's activities conform with the regulatory provisions, rules, procedures and codes of conduct.

SECRET 6

AN EFFECTIVE ERP SYSTEM IS THE BEST INVESTMENT YOU CAN MAKE!

Companies offer a wealth of information which, all too often, is not harnessed to full effect for the good of the company: in many businesses, the administration department works on Excel sheets which are often very complex, with information which at times is imprecise and lacking in updates.

The adoption of a **management controlling system**, even if simple in nature, **makes it possible to monitor** the **company's progress** in a precise manner, and to react promptly to any discontinuity in the market, whilst generating simulations that are more sophisticated, but at the same time easier to read.

Automating information processes is the most valid means of keeping all the management variables under control. Without these variables, the company's progress would be random in nature and uneven. Having them means we have detailed and precise control of all the aspects involved in the company:

- ✓ **The profitability** of the individual business lines, or of a specific geographical market;
- ✓ **The profitability** of a single product, a sales network, a new investment or a production unit;
- ✓ **The sustainability of the financial structure**, of the level of indebtedness and the stock of risk capital;
- ✓ The **size of the working capital** as a whole or its individual components (trade receivables, amounts payable to suppliers and levels of stock);
- ✓ **Cash flow trends**, allocation of **liquid funds**, and the intensity with which **credit lines are used**…

These are fundamental indicators which cannot be overlooked if we want to safeguard the continuity of the company and/or we are working to develop it.

Let's try to picture what consequences a vehicle speed sensor would have if it only measured your car speed approximately and with a time lapse. The car might exceed the speed limit along a stretch of road, but this information (even if correct) only reaches you five minutes later. The result: a guaranteed fine, and you can wave goodbye to your licence points. Or imagine a fuel sensor that only gives a rough idea of how much petrol is left in the tank, perhaps when the car has already ground to a halt having used up the last drop of fuel!

Exactly the same thing can happen at work: it is vital to know the margins of a given sale before it is concluded; it is vital to have an indication of a potential financial imbalance before the loss actually occurs; excessive stock levels need to be monitored minute by minute, and excessive growth must be stopped before it is too late.

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