How to Think Like a Digital CFO

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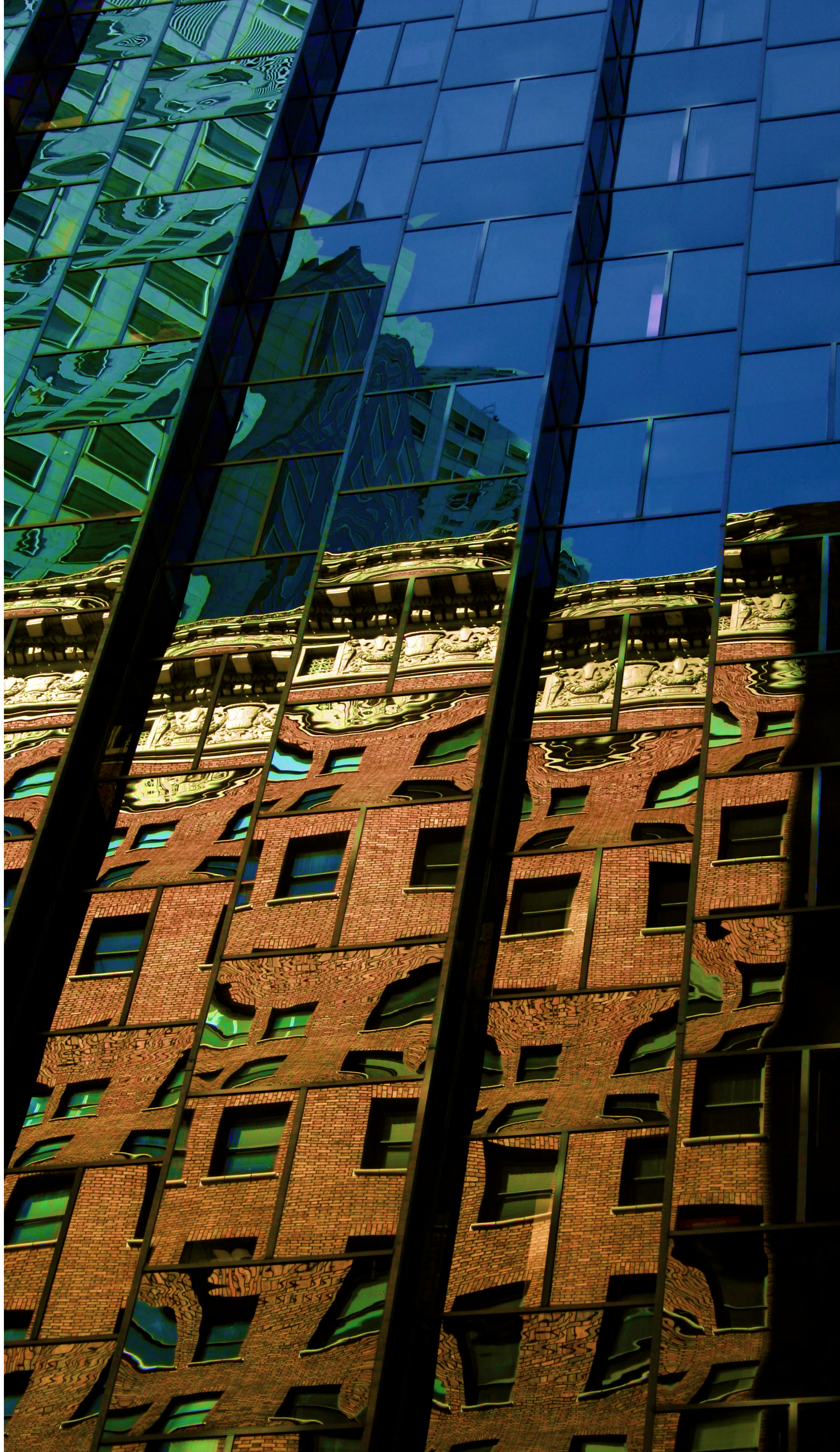
As we navigate the changes brought about by the digital revolution, we see the role of the enterprise CFO changing. In fact, the digital world requires us to think very differently about what a CFO does.

I'm not the first to notice this. Many articles in CFO journals, reports by consulting firms, and conference seminars have hinted at or described these changes. In the following pages, I assemble the thoughts of others along with my own to form a coherent way of characterizing the digital CFO.

My approach is to compare the "old" and the "new" ways of defining what a CFO does. These are very much generalizations—different CFOs and their enterprises have treated the role differently. When you put all these elements together, though, it's clear that the CFO has become central to driving the digital performance of the enterprise.



Old: Looked backward at trailing indicators and financial metrics

New: Looks forward at leading indicators and performance metrics

Traditionally, CFOs have focused much of their attention on financial reporting, which means, in a sense, that they have been looking in the rearview mirror. A financial report summarizes performance over a previous period, or, as with the balance sheet, summarizes the state of the business at the end of a period.

For today's CFO, of course, financial reporting is still critical. But technology makes it possible for the finance organization to get near real-time information about the company's performance, and even to gather data on leading indicators—those that show how the company will perform in the future. As Jeannette Wade, CFO of Ascentria Care Alliance, says, "The role of the CFO has changed from being the keeper of the financial information to the driver of business change with financial information."[1]

A variety of business intelligence and analytical tools can help the CFO slice and dice this information, and even perform predictive analytics through new machine learning technologies. Data lakes and real-time streaming make it easier for the CFO to analyze information across business silos, business units, and even subsidiary companies to gain a complete picture of the enterprise.

The digital CFO takes advantage of all these tools to make decisions and give the other CXOs insight into company performance.

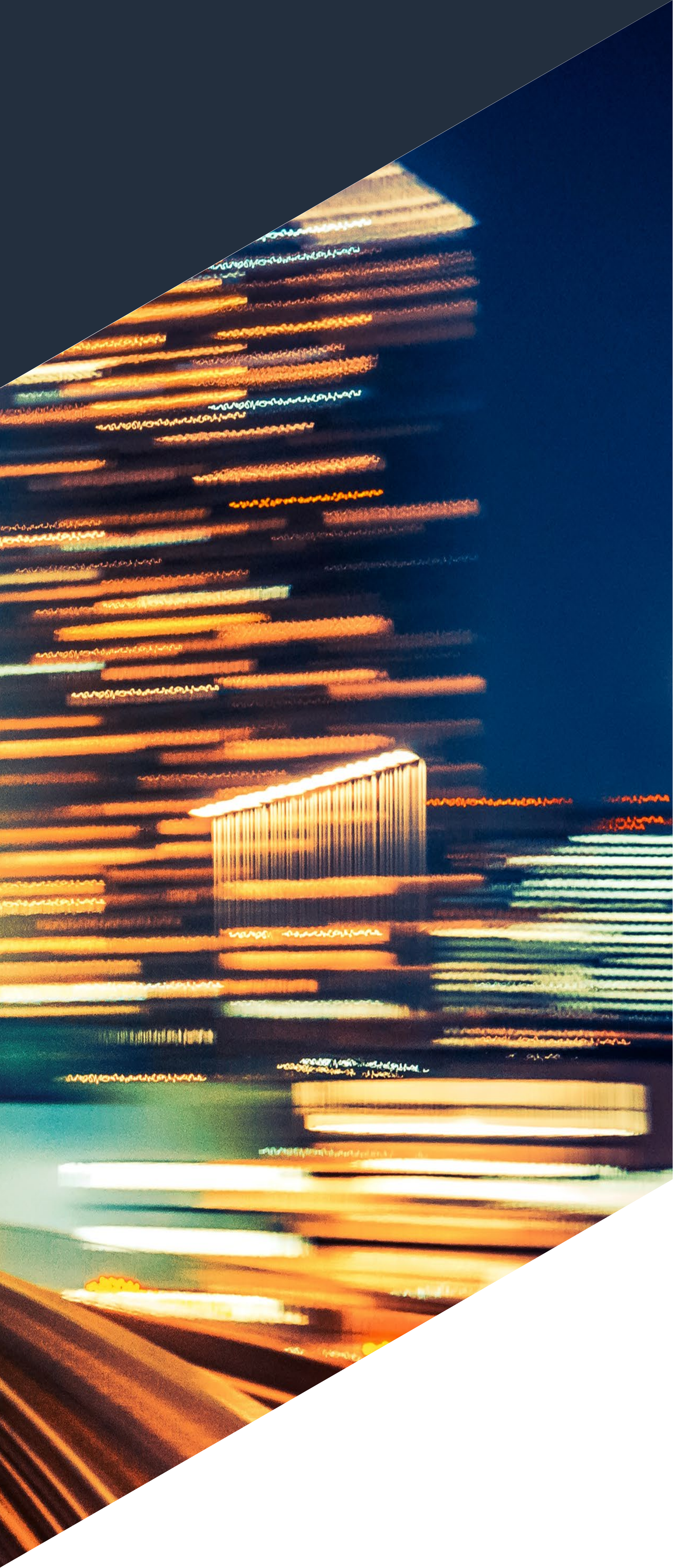
Old: Managed quarterly performance

New: Manages quarterly performance and invests nimbly

As steward for the board and shareholders, the CFO must make sure that the enterprise is future-ready and sustainable. Boards are increasingly worried about company sustainability as they see industries being disrupted and observe how precipitously companies drop from industry leadership positions.

Company sustainability involves a tension: on the one hand, the company must continue to innovate and grow, but on the other hand it must guard against risks to its core business as well as be alert to security breaches and market uncertainties. There is a "defensive" aspect as well as an "offensive" one.

The one certainty is that enterprises cannot sustain their market leadership positions through stasis, by maintaining the status quo, or by managing only for today, this quarter, or this fiscal year.



Old: Reduced costs

New: Manages costs while increasing growth

Eighty-one percent of CFOs believe it is their responsibility to identify and target new growth areas across the enterprise. CFOs must find and cultivate new sources of revenue.[2]

Though company sustainability is of key importance, the CFO cannot focus only on controlling and reducing costs. Maintaining a market leadership position in the current economy requires continuous innovation while seizing market opportunities as they arise. Boards and CEOs—not to mention the financial markets—demand growth, and the CFO must find a way to deliver it. That means spotting growth opportunities and directing cash and other resources toward them.

The CFO cannot be a naysayer; on the contrary, good financial stewardship means encouraging and supporting innovation and the spending required for growth. As AWS CFO Sean Boyle says, “Be a CF-go instead of a CF-no.”

Old: Focused on costs

New: Focuses on leanness

This subtle distinction makes all the difference in the digital world, which is a world of speed, responsiveness, and sustained feedback cycles. The enterprise needs to be fast in order to foster innovation, seize opportunities before competitors do, and respond effectively to customer needs.

By “fast,” I mean that lead times must be short. In the Lean Manufacturing/Toyota Production System paradigm, this means removing waste that contributes to long lead times. That waste might not be in obvious places—it’s often in bureaucracy, handoffs between business siloes, bureaucracy and redundant or ineffective controls, poor hiring practices, or feature bloat in IT systems (that is, “requirements” that shouldn’t be required). Fortunately, reducing waste also reduces costs, or at least unit costs.

I discuss this topic more in my eBook, An Executive View of Lean and Agile IT for CFOs.

Old: Guarded funds and resources, gatekeeping innovation

New: Channels funds and resources, accelerating innovation

Is the CFO one of many gatekeepers and guardians in the organization who vet innovations by saying “no” to most of them?

Or does the CFO help the company exploit potential growth opportunities by encouraging and saying “yes” to the right kind of innovation?

In a company with a growth imperative, it must be the latter.

Old: Focused on plans and milestones

New: Focuses on outcomes

In the old world, the CFO (and everyone else in the enterprise) focused on plans and adhering to milestones as a way to (ostensibly) control them and manage risk. But in an environment of uncertainty, plans must change often.

In any case, it’s not the plan that’s important—it’s the outcome.

In a world of short lead times and fast delivery (especially from IT), outcomes can be measured quickly and used as a control. The question should never be, “Did you complete all the requirements and execute according to plan?” Instead, it should be, “Are you generating valuable outcomes?”

Old: Deployed capital based on business cases

New: Deploys capital based on staged investments

Business cases prepared in advance of an investment are subject to uncertainty, complexity, and rapid change. It's risky to invest in a preplanned business case in times of disruption and volatility.

Fortunately, the digital world provides CFOs a better way to manage investment risk: through incremental, or "staged" (or metered), investment. Instead of committing funding to a large initiative, the enterprise can commit funding in stages.

IT teams can, and should, deliver results quickly and frequently (that's what DevOps is all about). The business results of these deliveries should be scrutinized as a way of deciding whether to continue funding an initiative, and at what level. It's possible to make small investments in a portfolio of opportunities and then decide which will yield the best returns before deciding which ones to commit funding to.

Old: Managed for sustainable competitive advantage

New: Manages for creative destruction and continuous reinvention

It's become very difficult to sustain a competitive advantage. Barriers to entry are low. Customers are fickle. Government regulations and policies change, as does the geopolitical situation. Distribution channels are disintermediated. Disruption is rife.

It may not be wise to depend on today's competitive edge to still exist when you wake up tomorrow. Today, companies compete based on continuous innovation, frequent reappraisal of business models, and creative destruction of existing advantages.

A CFO today is looking to create change, not to avoid it.

Old: Supported siloed activity

New: Supports cross-functional activity

Old-style budgeting and performance management were predicated on functionally siloed organizations. Marketing was responsible for marketing objectives and costs; IT for IT objectives and costs; business units for their own P&Ls. Today's organizational practices are based on cross-functional teams, the more widely representative of different functions, the better. The CFO must foster or create transparency across organizational silos and must find a way to fund and measure the performance of teams that cut across traditional organizational boundaries.

Old: CAPEX and fixed costs, total costs

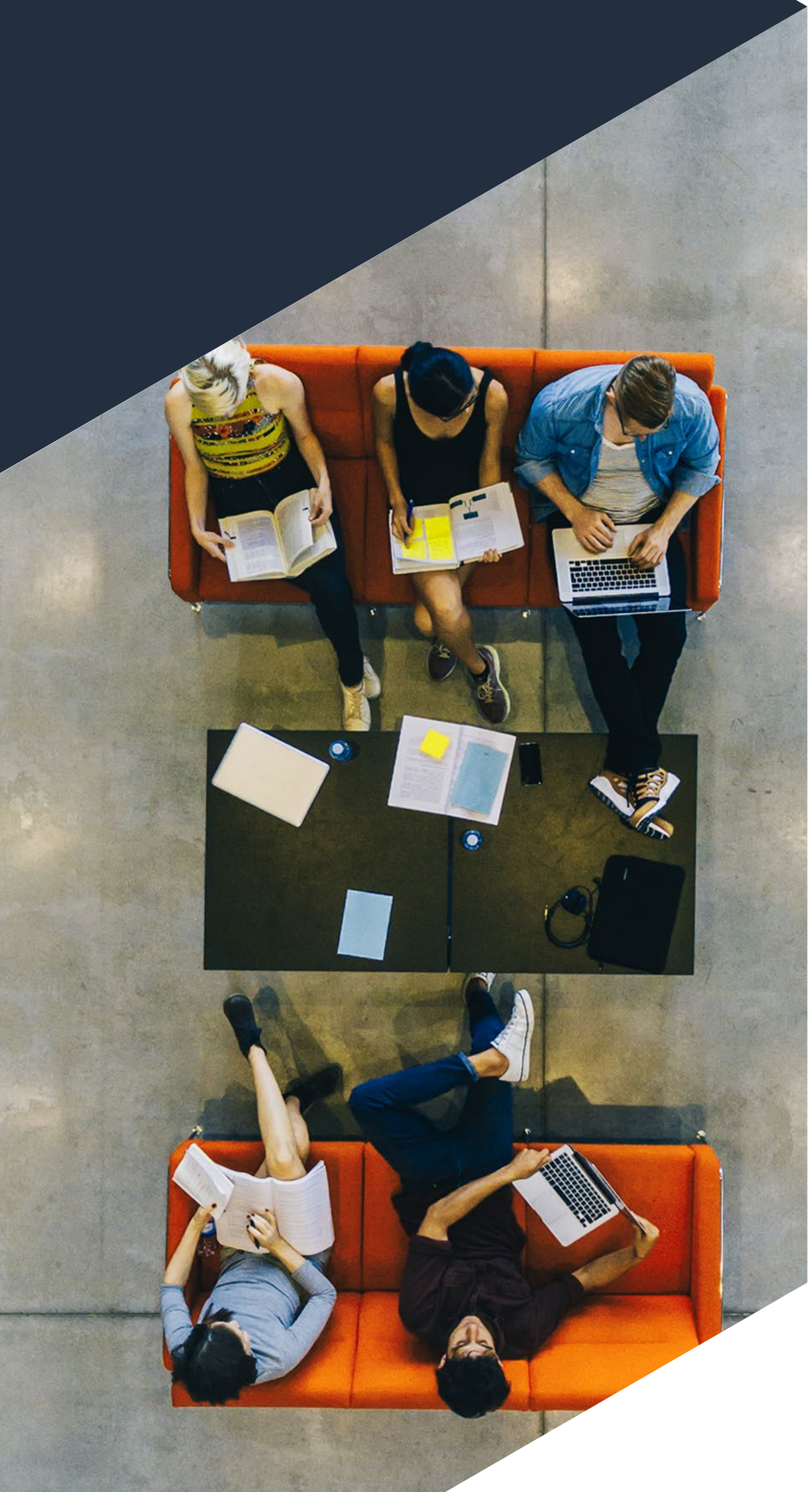
New: OPEX and variable costs, marginal costs

Enterprises can make better decisions in the digital world if they focus on *marginal* costs and *marginal* value, rather than total or average. The costs to operate a digital service are now typically variable costs. The cloud, for example, turns what used to be large fixed costs into small variable costs. DevOps breaks down monolithic IT system delivery costs into small incremental costs to deliver individual features or microservices.

This is one reason for lowered barriers to entry for startups: they no longer need large investments before they start doing business. Instead, they only see their costs rise as the business scales.

Traditional enterprises, too, can take advantage of this change to cost structure.

Often, these costs are expensed rather than capitalized. It's a mistake, however, to think of these techniques as *turning* capital expenses into operational expenses. Instead, most organizations find that when their capital expenses decline, their operational expenses decline as well because of increased efficiencies and reduction in unnecessary effort.



Old: Viewed IT as a cost center

New: Views IT as a partner and enabler

IT supports and enables the CFO in accomplishing all the changes I have discussed in these pages. Working with IT, the CFO can create transparency across silos, obtain near real-time data and analytics, reduce lead times, and divide investments into low-risk chunks.

But more than this, IT is an enabler of business growth and a driver of innovation, rather than just a fixed cost the enterprise must bear and try to minimize.

Old: Optimized finance operations

New: Optimizes cross-enterprise operations

According to a McKinsey study, two-thirds of CFOs think they should spend less time on traditional finance activities and more on strategic leadership.[3] In another study, BCG found that about thirty percent of the finance department's effort is invested just in the mechanics of assembling data and resolving inconsistencies.[4]

CFOs and their finance groups have spent entirely too much time on the mechanics of getting the books closed each month and the day-to-day work of running the finance organization.

The CFO is the CFO for the entire organization.

Old: Identified risk in unpredictability and managed only financial risk

New: Identifies risk in predictability and manages business risk

Status quo bias leads us to perceive risk in things that are new, while overlooking the risks in the old. Should you be more worried about the security of new techniques and technologies or the problems that exist in your security posture today?

Old patterns of thinking lead us to focus on cost and schedule risk when the real risk is not gaining the desired outcome at a good price quickly. Old patterns make us think that innovations are risky, whereas not innovating is even riskier. They convince us that it's risky not to follow an upfront plan and business case even when the environment is constantly changing, and new information is being discovered.

The CFO must bring to the enterprise a rational basis for making risk decisions and teach the enterprise to think differently about risk.

Old: Viewed compliance as a checklist (complied reactively)

New: Designs proactive compliance controls

The GDPR is, in many ways, a model for how we should think about compliance going forward. It requires that we implement "privacy by design." In other words, that we design customer privacy into our systems and processes as we create them.

This is indeed the way IT organizations increasingly think about security, resilience, and privacy: All IT systems should be designed for "ruggedness," or for the way they will be used and operated. It's not enough to make customer information secure against today's threats; tomorrow a hacker will invent a new way to steal it.

Similar considerations apply to other compliance frameworks—HIPAA, Sarbanes Oxley, FISMA. Instead of auditing after the fact to determine if there are appropriate controls, we need to design systems and processes so that they will meet the control objectives in a way that is resilient and future oriented.

In summary, these are traits I'm seeing in the new digital CFO:

- **Looks forward at leading indicators and performance metrics**
- **Manages quarterly performance and invests nimbly**
- **Manages costs while increasing growth**
- **Focuses on leanness**
- **Channels funds and resources, accelerating innovation**
- **Focuses on outcomes**
- **Deploys capital based on staged investments**
- **Manages for creative destruction and continuous reinvention**
- **Supports cross-functional activity**
- **OPEX and variable costs, marginal costs**
- **Views IT as a partner and enabler**
- **Optimizes cross-enterprise operations**
- **Identifies risk in predictability and manages business risk**
- **Designs proactive compliance controls**

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About the author

Mark Schwartz is a sought-after technology leader, prolific writer, and frequent featured speaker. He has held C-suite positions at several organizations, large and small, where over time he earned a reputation for consistently challenging the status quo in business, processes, and technology. Mark is an outspoken advocate for Agile and Lean methodologies and espouses a philosophy of continuous improvement. As an Enterprise Strategist for AWS, he uses his powers for good by collaborating closely with AWS customers to create and drive innovative cloud-based strategies.

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[1] https://channels.theinnovationenterprise.com/articles/expert-interview-jeanette-wade-cfo-executive-office-of-technology-services-security
[2] https://newsroom.accenture.com/news/cfos-play-a-major-role-in-digital-investment-decisions-across-the-enterprise-according-to-latest-accenture-research.htm
[3] https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/are-todays-cfos-ready-for-tomorrows-demands-on-finance
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