ACCA

Building the finance function in growing businesses

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The ACCA Global Forum for SMEs provides a unique platform for promoting the role of SMEs in the global economy. Representing over 15 countries and a wide range of professional backgrounds – from finance institutions, academics and professional advisers to entrepreneurs themselves – the Forum represents the sector's needs at a global level and facilitates the sharing of best practice.

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This discussion paper presents views and recommendations on how to build the finance function to support growth in SMEs. It takes a holistic view of the finance function, discussing a variety of issues from the roles it can play in a growing business to what investment is required.

ACKNOWLEDGEMENTS

This discussion paper is part of a wider collection of work produced by the Global Forum for SMEs looking at the experiences, challenges and opportunities presented by SME growth.

The Forum would like to thank the following for their expert contributions:

- Gary Cokins, founder and CEO, Analytics-Based Performance Management LLC
- Andi Lonnen, principal, ALBA
- Professor Stephen Roper, director, Enterprise Research Centre (ERC)
- Fernando Sepulveda, managing director, Impulsa Business Accelerator.

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INTRODUCTION

The global drive for economic recovery has placed a huge focus on supporting small and medium-sized enterprises (SMEs) as a vehicle for job creation, economic stability and wealth creation. Governments are also capitalising on the opportunities presented by SMEs for market innovation and its value in building social capital.

In order for SMEs to achieve their maximum impact, efforts to promote them cannot be limited to encouraging more of them to form; they have to be accompanied by efforts to understand and support the sustainability and growth of such businesses. Growth has many challenges; ACCA's 2014 report *The Growth Challenge*,[1] which examines the critical success factors for the policy and infrastructure supporting SMEs, highlights the reality that a large proportion of young SMEs fail to grow because of a lack of appropriate and timely support.

ACCA's research[2] has also demonstrated the importance of an evolving finance function and its symbiotic relationship with the growth of a business, from its informal setting-up of processes and systems onwards.

This discussion paper contributes further to this discourse, adding practical insights from members of the ACCA Global Forum for SMEs: experts who have experienced and supported growth first-hand.

THE GROWTH PIVOT

Finance functions of growing businesses differ from those of more static businesses in that more of the information that is most crucial to management is external rather than internal to the business. Therefore the finance function needs to pivot quickly from an inward-looking to an outward-looking function that is capable of monitoring market trends and the changing political and regulatory landscape, and benchmarking against the competition, the sector and good practice. This has implications for the skill needs of the business, as this 'pivoting' is more difficult for a finance function with a narrow skill-set that does not encompass elements of strategic planning and management accounting.

PLANNING FOR GROWTH, NOT FOR THE BANK

Growing businesses' new-found need for flexibility profoundly alters the mechanics of business planning. Many SME business plans are static, formal documents that were developed as a one-off exercise when the business was seeking external finance. While these are far from optimal for any business, they are even less adequate for growing SMEs that may go through many changes in a relatively short period of time. The business plan will also vary depending on whether the intended audience is internal or external.

For a growing business it is likely that what is needed is a less formal 'living document' that is not necessarily presented in a traditional document format (it could be produced as a presentation, for instance). The function of which will be to align everyone's efforts in the relatively short and medium terms and keep everyone up to date and focused on current objectives.

Data structures and systems will often require greater attention in a growing business than in a static one, and provisions for data-mining and analysis should feature in the business plan. Only with accurate and real-time information can management see how the business is performing, and identify gaps and opportunities.

A crucial difference between static and dynamic business plans is the need to allow for a shifting market in the latter – after all, it is often the fluidity of the market that makes it possible for the business to grow fast in the first place. The business plan of a growing business cannot assume that the market is constant in size, structure or customer preferences, and must assume that the business's actions will prompt reactions from competitors. Internally, the dynamic business plan needs to anticipate a life cycle for the business's products and services, and acknowledge that periods of rapid growth may shorten these.

Business plans will also need to keep tabs on cash flow, ensuring there is alignment and balance between both short-term and long-term funding. The obvious result is that key performance indicators (KPIs) need to be adjusted much more frequently, and flexibility must be built into the business plan, especially in relation to future developments.

INVESTING IN FINANCIAL CAPABILITIES

Resource acquisition and infrastructure constitute a key challenge for the finance function of a growing business. The business needs to build and hold resources that it may not be using currently (including, but not limited to enterprise resource planning (ERP), customer relationship management (CRM) and other IT systems, as well as

1. *The Growth Challenge*, ACCA, 2014, http://www.accaglobal.com/content/dam/acca/global/PDF-technical/small-business/pol-tp-tgc.pdf

2. *Driving SME Growth Through an Evolving Finance Function*, ACCA, 2012, http://www.accaglobal.com/content/dam/acca/global/PDF-technical/finance-transformation/pol-afb-dsgt.pdf

finance staff) or may be using at less than full capacity for an uncertain period of time, in anticipation of further growth. Finance leaders need to work out the appropriate balance between investment for the future and managing day-to-day operations and expenditure, in order to be able to justify this to the business.

To ensure timely investment, the finance team needs to be open with the rest of the business about where the cracks in the systems are beginning to show, without fear that this will reflect on their own performance. Such 'cracks' are typically measurable in terms of the accuracy of records, and the amount of ad hoc work and reconciliation it takes to provide information to the standard required.

This information can then be used to estimate the anticipated cost savings that should result from acquiring new resources. The same information can be used to demonstrate what new opportunities could be exploited when obtaining timely information is an option, and the extent to which this could provide the business with a competitive advantage. As with all small businesses, payback times are usually as, or more, relevant to management as estimates of return on investment. As well as factoring in opportunity costs, it is crucial that investment decisions factor in the cost of failure; finance leaders need to work out whether such costs are affordable and how such risks can be mitigated.

Data infrastructure is a particularly important type of resource, as a growing business needs to be able to perform data mining and have access to actionable real-time information. Data mining capabilities typically generate good returns, but realising these depends strongly on both communication with internal business partners and robust policies.

A particular danger for businesses facing strong but uneven growth is the temptation to outsource a lot of their IT infrastructure. As a minimum, growing businesses must allow for a period of parallel running of old and new systems when adopting any new systems.

Moreover, the business case for outsourcing needs to anticipate the business's growing demand for up-to-date information. When third parties are unable to manage the frequency of information requests generated by a rapidly growing business, the result can be substantial downtime and data loss from which the business may not be able to recover.

Businesses that are self-sufficient in information management can be more robust to outside challenges, but must also juggle the security and data protection obligations that a third-party supplier is likely to be able to handle more easily.

Finally, it is important to appreciate that systems and technology are only complements to the skills of in-house staff. Unless both are developed in tandem, growth will most likely come at the price of staff turnover, overworking, and stress.

BUILDING FINANCE LEADERSHIP

Rapid growth cannot be sustained without moving on from simply employing accountants to developing financial leadership. This is a particularly important lesson for a business growing rapidly from a very small size, where the finance director will probably have worked alone or with only very junior subordinates. Indeed, while larger organisations can count on recruiting finance leaders internally or externally, smaller businesses may need to develop and nurture junior employees into the role.

In keeping with their broader role, finance directors or CFOs in growing firms need to build greater communication, influencing and leadership skills, and take an active interest in the governance of the organisation – where challenges are bound to arise as the business may outgrow the original founding team's vision and visibility.

Elements of governance that can appear irrelevant in a steady-state business can quickly become crucially important when the business starts to grow rapidly. For a high-potential business, good governance coupled with appropriate communication channels and policies can be liberating, as it redirects resources previously tied up in excessive management controls, 'back-covering' and politics to the true objectives of the business. Its function is to free people, allowing them to work without fear. Finance leaders have a role in promoting this.

The above does not mean that all relevant knowledge and insights need to reside with the finance leaders from day one, or that such assets will always be accessible to them; growth creates endless distraction for finance leaders, who need to acquire 'sounding boards' in response; non-executive directors with experience of other industries are a good place to start. External advisers such as accountants are also a useful source of information, especially as the accountant will be able to draw on experiences working with other businesses.

Finally, finance leadership requires delegation – not simply in order make the CFO's role manageable, but to release finance staff for value-added work as business partners. Hence ahead of a major growth episode the finance function needs trusted key support staff to whom the CFO or finance director can delegate effectively.

THE FINANCE DIRECTOR/CHIEF FINANCE OFFICER AS BUSINESS PARTNER

Fast-growing businesses can easily fail if they lack clarity on how rapid order growth can be turned into sustained profitability. Finance needs to take on the role of ensuring fulfilment, particularly ensuring that suppliers and working capital are in place, and matching long-term resources to long-term needs and short-term resources to short-term needs.

This often requires a major departure from past working practices as the finance function can be isolated from the rest of the business. For static businesses, this attitude may be sustainable for some time, as it represents an equilibrium in the relationships between functions, but in fast-growing businesses this equilibrium breaks down and the finance team needs to become intimately involved in the growing business to understand its detailed workings.

Innovations that may disrupt the low-performance equilibrium of static businesses can include a new-found emphasis on cost-cutting through improved efficiency, often triggered by harnessing technological change or adopting new lower-cost business models, the effective use of resources and finance, and the need to be willing to cannibalise or move on from existing, historically successful products.

The finance staff cannot support or influence these decisions if they do not know and monitor the business well enough. Hence the finance function of a growth business needs to work in close partnership with operational parts of the business, and the CFO needs to understand the business in its totality. Particularly important is the need to liaise with the supply chain, including both suppliers and the operations staff who would normally deal with them.

Of course, understanding needs to flow in both directions. Finance leaders need not only to raise awareness of the finance function and its work among their colleagues but also to nurture among their staff awareness and respect for the work that the rest of the business does.

THE FINANCE FUNCTION AS INFORMATION HUB

Growing businesses are hungry for information. It is very hard for any business to grow substantially without innovating, accessing new market segments or exporting to new geographical markets, all of which introduce a measure of the unknown into business planning. Assessing these risks requires a finance function that can stay aware of the shifting market, as well as the domestic and customer economies – even the political situation in many countries where political or regulatory risks are important.

A growth episode will tend to be the first time that a finance director/ CFO needs very up-to-date, even real-time, information. It becomes a necessity not just for performance management but also in order to provide useful clues about the business's changing environment. Such episodes also bring to the fore any gaps in the knowledge of entrepreneurs themselves – often on fundamentals of financial management or the inner workings of suppliers or customers.

Meanwhile, high-potential businesses are offered a wealth of government support and incentives, are sought after by a significant network of alternative finance providers, and are subject to increasingly complex regulation and tax rules, especially once they start operating across borders.

While external support and information for dealing with choices and challenges is usually available, it is typically heavily fragmented and varies in quality and user-friendliness. Hence, without substantial guidance, the pursuit of support and compliance can grow into a major distraction that the growing firm cannot afford. For many growing businesses, an accountant (whether in-house or external) is the only link to a professional network or government support infrastructure beyond their immediate locality. It is part of the skill set of professional accountants to be able to act as a clearing house of information on business support partnerships.

Finally, 'growth businesses' face particular challenges when seeking external finance, especially so when looking at alternatives to the most traditional sources of equity or credit, or finance for exports, which is generally harder to secure. They also face behavioural constraints, as fast growth is often best financed through equity, with which business owners may be reluctant to part. Here, the finance function's role as an information hub also needs to be augmented with a coaching and mentoring role to ensure that the business is investment ready, and business owners can make informed decisions about accepting outside creditors or investors.

KEEPING THE GROWTH ENGINE RUNNING

Much of the discussion on business growth assumes that growth is potentially an option for businesses at all times. This, however, is not the case. Most growth windows are short-lived unless the business adapts to exploit them in the long-term. The business cycle turns; competitors recover and adapt. Finance leaders need to be conscious of the timing of growth and separate short from long-term effects in their business planning.

Updating the business plan on the basis of external inputs and an appreciation of growth timing is a continuous learning process that needs to be owned by the finance function. In practice a continuous process of re-alignment of resources and renewal of commitment needs to be embedded into the culture of the business. Growth can run out of steam quickly or become derailed when governance and information processes are not scalable. Stability can become very appealing after years of rapid growth, long hours and personal sacrifices. Staff, and even owners themselves, can grow weary or out of their depth, and their skills can become redundant.

When growth is uneven, ensuring sustainability requires constant vigilance from the finance function. Keeping a close watch on cash flow and doing regular cash forecasting is crucial, and funding for both working capital and development needs to be replenished in line with business plans in order to ensure that lack of funds does not become a barrier to growth. More complex is the challenge of maintaining customer care once the business is on a rapid-growth trajectory, as loyal customers can easily be overlooked. By building into business plans and KPIs reasonable assumptions about customer loyalty and the cost of servicing versus the cost of acquiring customers, the finance function can help focus attention on loyal customers as well as new sources of demand, or at least allow the business to make conscious, strategic decisions about how to balance customer retention and acquisition.

BUYING VERSUS BUILDING FINANCIAL CAPABILITY

The consensus is that commercially sensitive information and information that is required for the day-to-day operations of a business need to be kept in-house, as do the means of producing this information. This ensures both that third parties cannot exploit the information against the business and that actionable information can be produced quickly.

It is worth noting that owing to the lack of diversification in small, growing businesses' operations, financial information can often be much more revealing to outsiders than would be the case for a larger, more complex business – crucial information on profit margins, for instance can often be very transparent.

Clearly, depending on the business sector, the list of 'core' functions that must be kept in-house can vary. As a rule, however, budgeting, cash, order book, trade credit and customer-related information are best kept in house, while risk management is virtually impossible to outsource.

That said, there is a difference between process outsourcing and infrastructure outsourcing that the finance function needs to understand and convey to the business. Using cloud services or Software as a Service (SaaS), much of the business's infrastructure can be outsourced to provide crucially important scalability, while the business retains real-time control of all inputs and outputs. It is process outsourcing that is much more problematic unless the tasks are low risk and routine, for example, payroll management.

RECOMMENDATIONS FOR BUSINESSES

Design the business plan to be a 'living document'
This business plan should focus on aligning everyone's efforts in the relatively short and medium terms while being the central point for updates on any changes and developments. The business plan must be able to adapt to the fluidity of the markets within which the firm operates.

Invest in data infrastructure
A growing business needs to be able to perform data mining and have access to actionable real-time information. This information will also reveal where the cracks and gaps are as the business goes through rapid growth.

Focus on balancing the benefits of outsourcing with the need for self-sufficiency through building in-house capacity
Both must be developed in tandem to ensure growth that is robust against external challenges.

Develop strong financial leadership
This may require building a network where advice can be readily sought, for example, the board, support staff and external advisers.

Finance leaders must start acting as business partners
Getting intimately involved with the day-to-day workings of the business will help CFOs and finance directors to make informed decisions and understand the whole impact that such decisions will have.

Grow the finance function to become the central information hub for the business
This will enable the finance function to consolidate, synthesise and disseminate information to where it is required, be it to meet new regulatory and compliance targets or to inform new activities such as exporting. Using external advisers such as accountants, who can act as clearing houses for business support, is an effective approach to building this information hub.

Understand what growth will look like for the business over the long term
Businesses do not all experience growth in the same way. It is important to monitor how growth may be affected by factors such as where it occurs in the business cycle, market changes and finances. It is also crucial to understand the effect that growth may have on the business, including staff fatigue and effects on customer bases.

RECOMMENDATIONS FOR POLICYMAKERS AND BUSINESS SUPPORT

Facilitate the creation of, and access to, professional networks
This should include access to accountants, finance providers and business mentors to support businesses looking to grow. For those businesses seeking to export, this facilitation should also include easier cross-border exchange of information, especially on tax regimes.

Develop incentives to encourage businesses to invest in data infrastructure and processes
This could include upgrading or outsourcing IT software and systems, recruiting data specialists or undertaking training to build in-house capacity to perform tasks such as data mining and analysis.

Support business in crafting business plans that are fit for growth
This means more than simply turning out a paper document, and requires the business to be financially educated so that it is able to perform the whole range of tasks that are typically part of growth, including accessing external finance, diversifying the business model and so on.

Conduct research to identify the range of different growth scenarios that businesses may go through
Paying particular attention to the various types and level of support that businesses may require according to characteristics such as size, sector, markets, etc. For example, where as some businesses will require support in accessing markets, others may require support aimed at developing the leadership team.

Ensure that finance markets (including electronic banking and mobile money) are working efficiently
It is vital that growing businesses can gain access to the finance that they need to support growth, whether this is equity or loan capital or the need for secure money transmission services.

Address the high level of risk associated with innovation through incentives and initiatives
Unlike larger companies with a portfolio of businesses, SMEs are generally unable to diversify away the risks associated with innovative activities. Hence it may be necessary for governments to support innovation (for which SMEs are acknowledged to be an important source) so that innovative activity rises to the level that is economically desirable. Such support can include tax incentives, underwriting of risk capital funds, loan guarantee schemes and promotion of a vibrant market for crowdfunding.

Ensure that SMEs have access to fast, secure and affordable broadband and network services
The value of technology to conducting business has grown significantly over the past decade. Easy and affordable access to the internet, cloud services and infrastructure (eg SaaS), and e-commerce and m-commence trading platforms should be considered frontline support for businesses looking for growth.

Ensure that regulation and compliance regimes are proportionate, efficient and low cost as possible
Compliance should not result in a disproportionate amount of SMEs' scarce financial management time being spent on bureaucratic procedures or dealing with multiple government offices. Larger firms tend to have the depth of resources needed for this, but SMEs do not, potentially placing them at a disadvantage.

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