Cost of Control:
‘Fuzzy Finance’

Research Report

November 2011

basware

Contents

Foreward

Since 2009, Basware has undertaken research under the banner of 'Cost of Control' to establish how finance professionals intend to solve the problems of cost saving and profit margin improvement via Purchase-to-Pay networks. In 2011, we see these problems described in an entirely new way.

Rarely can a CFO look at their financial organization with complete satisfaction and confidence that current workflows, processes and networks are optimised. In the past decade, this may have been attributed to something purely technological, an absence of 'dialogue' between disparate systems or the need to replace manual processes with automation. However, with an increasingly interconnected organization, the issue today is how to best integrate and optimise in a continually changing internal environment. Findings from the research show that the automation and integration of financial processes is a continually moving target.

What was once a purely technological problem is now described by a seemingly endless series of interdependent workflows that impact operational efficiency. The Purchase-to-Pay (P2P) environment was defined as a measure to bring seemingly integrated but mostly siloed aspects of the procurement and financial payment processes together. As a business process, and as a technology, P2P has matured over recent years. However, the problem that P2P seeks to address is continually evolving as financial professionals look to generate greater cost savings and efficiencies from the business critical process of 'paying the bills'.

P2P networks accommodate suppliers, payment records, materials, services, financial transactions and organizational cashflow. In fact, outside of the payroll, P2P is considered by respondents to be the most significant aspect of cashflow management within a large organization. Moreover, the P2P network operates inside and outside the organization, an environment far more complex than an employee-driven (payroll) infrastructure. It is for this reason that the P2P is considered by Basware to be the most important set of commercial interactions within an organization and a keystone to unlocking future business efficiency.

Within the research, financial professionals clearly state a consensus around three key areas: the significance of e-invoicing as solution to drive cost savings, the increased importance of accounts payable as function that impacts the wider financial organization and the complexity created by interdependent financial processes into a network of records and events.

In conjunction with these acknowledgements, the research describes 'rigidity' in finance confidence over its departmental capabilities, and challenges surrounding accuracy and visibility of financial information. It is our contention in the report that these factors are related. CFOs are placing greater importance upon budgeting, reporting and cashflow, whilst the environment they look to control becomes tougher and more complex. This affects the financial organization's ability to meet its own expectations and that of the wider business.

One single solution can no longer be seen in isolation of others within the business and a change at one end of the financial spectrum almost certainly will alter the requirements at another – but no longer just as a workflow. Now, CFOs are waking up to the issue of how, on the one hand, a payment record represents a piece of paper that can be automated, whilst on the other it represents much more. It is an accountability tool, a connection to an array of supplier relationships, of taxation considerations and even of currency exchange requirements.

In this context, the findings in the following report should provide readers with thought provoking insights and inform the debate of how financial excellence is maintained in an increasingly networked world. The parallels with current international capital markets are appropriate. Whilst the presence of 'fuzzy finance' within organizations may lack the 'calamitous' implications of a global financial crisis, it appears that many CFOs are struggling to control the complexities of the financial processes within their own domains.

Executive summary

The 2011 Cost of Control research highlights key trends shaping financial decision making across Europe, America and Australia. It is the third year that research of this kind has been commissioned by Basware following similar studies in June 2009 and May 2010. The key findings from the survey are summarised as follows:

- Financial process present complexity challenges as a result of increased levels of interconnected records, relationships and events
- The disruption of cashflow visibility and cash management due to interdependent 'networks'
- Increased importance of e-invoicing and accounts payable within large organizations
- Levels of confidence and satisfaction aligned to cash management and payment processes

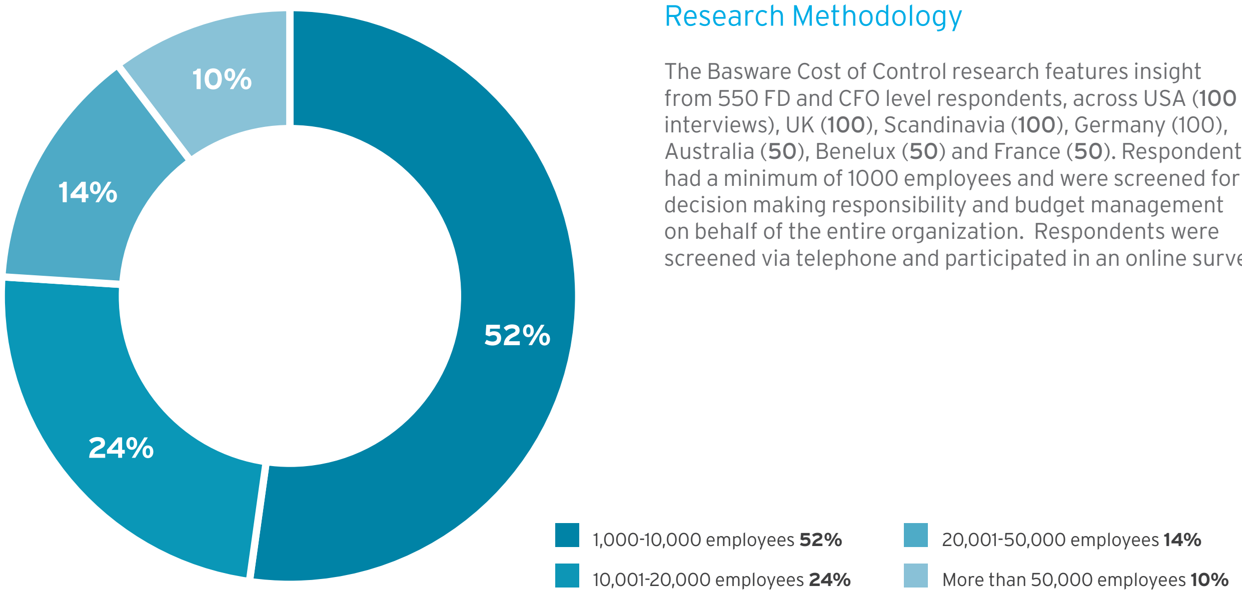
This research provides a temperature check on CFO confidence and financial department capabilities and concerns in the last quarter of the calendar year. It was undertaken at a time when Eurozone uncertainty and static growth are defining macro economic thinking, whilst banking infrastructure continues to realign itself post the 2008 recession. In short, it is a time of fundamental financial change. Company-specific performance and sentiment is somewhat decoupled from these far reaching economic trends as business adopt strategies that respond to the 'new normal' of global commerce. The key findings of the Cost of Control 'Fuzzy Finance' survey can be summarised as follows:

The Network Effect:

- 69% of respondents think changes within one part of their finance infrastructure are more likely to impact other parts of their business due to increased systems interdependencies
- 79% agree understanding the impact of new systems and processes on the wider organization is important when seeking operational efficiencies
- 59% think decisions have been made within their business to improve financial operations without a clear understanding of the wider implications on cash flow visibility

Cashflow Clarity:

- 71% of respondents agree that greater levels of reliance between different finance systems within their organization today present cash flow visibility challenges
- 55% think it is difficult to get a detailed picture of the company cash flow position on a real-time basis
- 83% of customer invoice and payment systems, and 84% of supplier payment systems are not fully optimised* within organizations



Research Methodology

The Basware Cost of Control research features insight from 550 FD and CFO level respondents, across USA (**100** interviews), UK (**100**), Scandinavia (**100**), Germany (100), Australia (**50**), Benelux (**50**) and France (**50**). Respondents had a minimum of 1000 employees and were screened for decision making responsibility and budget management on behalf of the entire organization. Respondents were screened via telephone and participated in an online survey.

This research provides a temperature check on CFO confidence and financial department capabilities and concerns in the last quarter of the calendar year.

Accounting Ascendance:

- 64% believe the accounts payable function today has a more immediate impact on other parts of the business due to higher levels of integration between systems
- 68% of businesses think greater levels of e-invoicing and payment automation would improve cash flow visibility for their organization
- 62% agree inefficient accounts payable practices compromise cashflow visibility

Confidence Clash:

- Whilst confidence in company performance is improving, financial department confidence remains unchanged
- Concerns around the performance of cash management and cashflow visibility hinder finance sentiment
- Strategic priorities for 2012 are driven by revenue forecasting (64%), topline performance (59%) and cash management (55%)

The research describes two concerns; 'networked' finance challenges and cashflow visibility issues, whilst also showing the increased importance of financial process optimization and doubts surrounding the sentiment of CFOs against general finance performance and cash management. These factors will be related for a large number of respondents and the question of how best to improve on the present situation will form part of strategic planning activity for CFOs as 2012 beckons.

(*rated performance as less than '5' on 1-5 scale where 5 represented fully optimised)

69%

think changes within one part of their finance infrastructure are more likely to impact other parts of their business due to increased systems interdependencies

71%

agree that greater levels of reliance between different finance systems within their organization today present cash flow visibility challenges

64%

believe the accounts payable function today has a more immediate impact on other parts of the business due to higher levels of integration between systems

Strategy & Confidence

Over the course of the last year, the strategic corporate landscape has changed considerably. The business focus is now less on 'defend and protect' and instead is replaced with a more focused approach to managing the financial operation.

Over the coming 12 months 'reducing overall purchase costs' (**-8%**) and 'maintaining and improving margins' (**-6%**) both decreased as the main priorities amongst key financial decision makers, compared to 2010. In their place have emerged priorities more focused on financial management. The top concerns over the coming year include planning, budgeting, and revenue forecasting (**64%**), increasing profits and top line performance (**59%**) and cash flow and working capital management (**55%**), all of which have increased as a priority since 2010.

Challenges remain, however, surrounding the implementation of these cash management and cash flow visibility strategies. The main barriers affecting finance functionality include finding operational efficiencies within the organization. Difficulties in realising costs savings across the business (**48%**) and in identifying cost saving opportunities (**42%**) emerge as the main concerns for businesses (**see Fig 1**). Realising cost savings across the business is a particular challenge in both France (**58%**) and the US (**53%**). Further challenges lie in fully integrating company-wide systems and the difficulties this creates with new technology (**47%**). Such concerns are particularly evident in France (**60%**) but less so in Benelux (**34%**).

Optimism amongst the business world is on the up. CFO confidence in their own company performance increased **7%** over the course of the year to **51%** (**see Fig 2**). Such confidence was highest amongst German companies (**72%**), whereas Australians were less optimistic (**20%**). Despite an overall increased optimism, confidence in the performance of the financial function remains unaffected, levelling at **50%** a year on. This is reflected in having an understanding of cash flow and invoicing status at all times (**46%**), which remained unchanged from 2010. Both the UK (**41%**) and Australia (**22%**) show the least assurance in their own finance function, but both France and Germany (**64%** and **60%** respectively) display a greater optimism.

FIGURE 1: Significant challenges
Which of the following are more significant challenges affecting finance within your company now compared to 12 months ago?

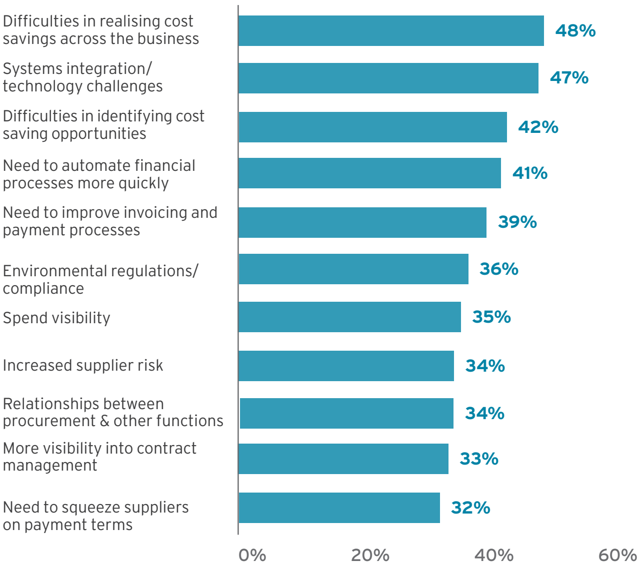
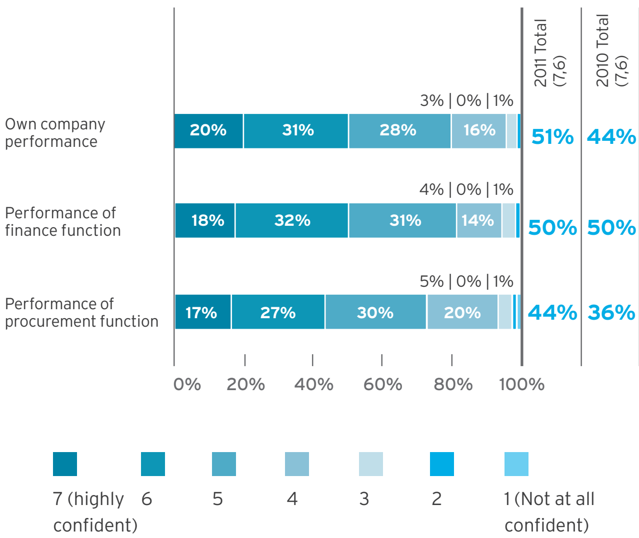


FIGURE 2: FD confidence
Using a scale of 7-1 where 7 is "highly confident" and 1 is "not at all confident", how would you rate your confidence in the following at this point in time?



The Network Effect

Inter-business connectivity is ever growing in the modern workplace. In the past where individual business departments would function autonomously from the wider organization, now there is a greater reliance on interdependency in order for the business to succeed.

With such reliance across the organization, the structure of the financial system is pivotal in keeping the ship steady. Two-thirds (**69%**) of respondents think changes within one part of their finance infrastructure are more likely to impact other parts of their business due to increased systems interdependencies (**see Fig 3**). This is more prominent in both the US (**78%**) and France (**78%**) and highlights the sensitivity of the wider business to changes within the finance system and vice versa.

Whilst internal systems across the company become increasingly reliant on each other, there is also a need to fully understand the effects that new procedures and practices have on the wider business. Such knowledge is seen as central to enhancing the business' productivity. **79%** agree that understanding the impact of new systems and processes on the wider organization is important when seeking operational efficiencies (**see Fig 4**). This view is advocated by German business (**89%** agree) and also by US organizations (**86%**). It is therefore imperative that businesses as a whole fully understand these new practices and are in essence 'reading from the same page'. Any ambiguity or misunderstanding on financial processes within an ever reliant network can be costly for an organization, particularly in terms of monetary visibility.

59% think decisions have been made within their business to improve financial operations without a clear understanding of the wider implications on cash flow visibility (**see Fig 5**). Despite the vast majority of US organizations agreeing on the importance of understanding the impact of new processes on the wider organization, 3 in 4 US companies (**75%**) claim financial decisions have been made without a clear understanding of the wider implications on cash flow visibility.

FIGURE 3: System Interdependencies (agree/strongly agree)
Changes within one part of our finance infrastructure as more likely to impact other parts of our business due to increased systems interdependencies

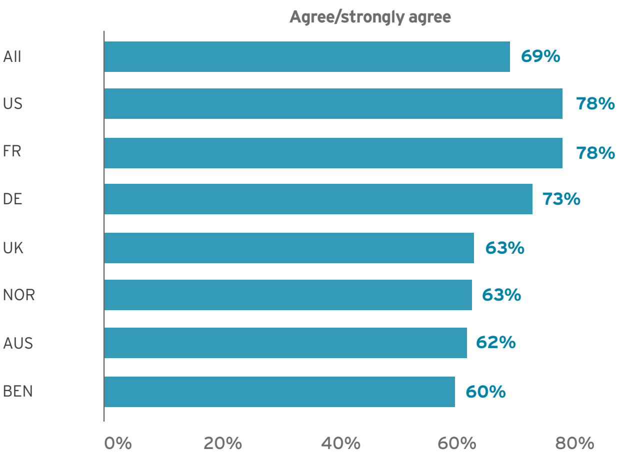
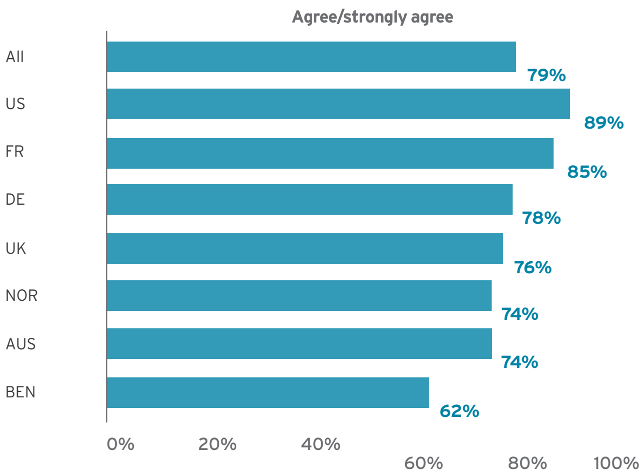


FIGURE 4: Impact of new system and process (agree/strongly agree)
Understanding the impact of new systems and processes on the wider organisation is important when seeking operational efficiencies



Cashflow Clarity

With an increasing integrated network and high business interdependency, it perhaps not a surprise that the financial infrastructure faces numerous obstacles. One of the key challenges to overcome is keeping all interested parties updated and ensuring cash-flow statuses and necessary outgoings are clear.

71% of respondents agree that greater levels of reliance between different finance systems within their organization today present cash flow visibility challenges. Both German and French businesses are more likely to agree (**83%** and **82%** respectively) that these cash flow visibility challenges exist. As uncertain economic conditions continue, the need for such clarity is as ever important. Financial decisions now have to be made in a quick paced environment, where having all the relevant and up to date information may not always be guaranteed. **55%** think it is difficult to get a detailed picture of the company cash flow position on a real-time basis. This is especially so in Germany, where two-thirds (**66%**) of companies agree with these difficulties.

Consequently when cash-flow clarity is put under strain, the payment processes is likely to wane. **84%** of business' supplier payments and **83%** of their customer invoicing & payments are considered to be not fully optimised. Only utilities & direct spend are considered to be worst off in their optimization (**89%**). Such payment inefficiencies and cash flow ambiguities clearly present challenges for companies.

Nearly two thirds (**68%**) of businesses believe that customer invoicing & payments are creating the biggest challenge for their organization. These are bigger concerns amongst US and UK companies, where **77%** and **73%** of businesses respectively see this as an issue. Similarly, **61%** of businesses feel supplier payment presents a current challenge, again more so in the US and UK (**68%** and **66%** respectively). It therefore appears that cash flow visibility and efficient payment processes need to effectively co-exist to ensure the successful functioning of the financial system

FIGURE 5: Cash flow visibility (agree/strongly agree)
Decisions have been made within our business to improve financial operations without a clear understanding of the wider implications on cashflow visibility

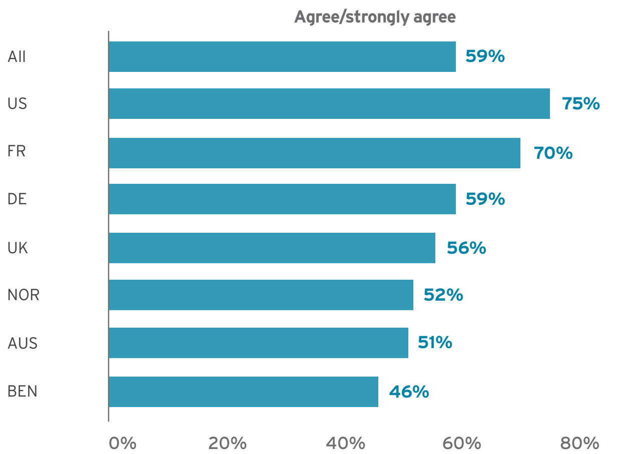
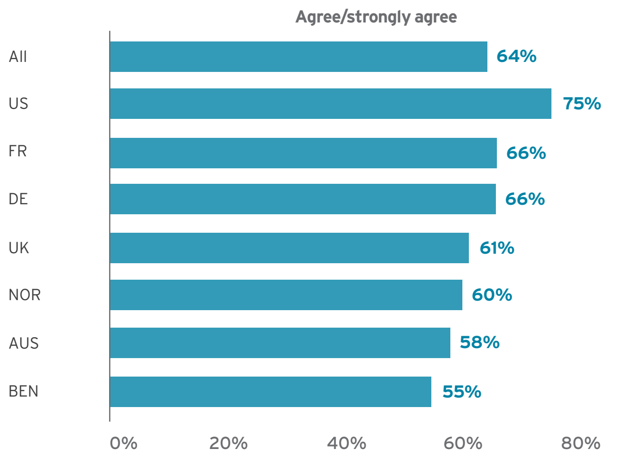


FIGURE 6: Accounts payable function (agree/strongly agree)
The accounts payable function today has a more immediate impact on other parts of the business due to higher levels of integration between systems



Accounting Ascendance

Improving the accounts payable process has become increasingly important in an era of tightening credit where adequate cash flow and greater control over company payables are vital in maintaining liquidity and sustaining business operations.

In today's business environment where a network of reliance is prevalent and cash flow visibility integral to efficiency, the accounts payable process also has a unique ability to ensure all these areas are successful. **64%** believe the accounts payable function today has a more immediate impact on other parts of the business due to higher levels of integration between systems (**see Fig 6**). As previously seen, the effects of system integration are more established in the US and consequently 3 in 4 (**75%**) US businesses recognise the immediacy of this impact. Nordic countries are less convinced of this connection, with just over half agreeing (**55%**).

As discussed there is a connection between the importance of the accounts payable function and the integration of systems, yet similarly the success of the payment process can have an effect on the visibility of the cash flow. **62%** agree inefficient accounts payable practices compromise cash flow visibility (**see Fig 7**). Once again, this highlights the relationship between an efficient payment process and clarity of cash flow. US (**73%**) and French (**72%**) companies are more likely to believe that a compromise exists, whereas Benelux (**50%**) and Australian (**50%**) businesses are less convinced.

In order to support the accounts payable function and reduce cash flow uncertainty, the majority of finance departments are looking to incorporate e-invoicing into their process – just under two-thirds (**68%**) of businesses think greater levels of e-invoicing and payment automation would improve cash flow visibility for their organization (**see Fig 8**).US businesses (**84%**) are more likely to hold this view, followed by French businesses (**78%**). E-invoicing is now top of businesses' 'to-do' list – over half of companies (**52%**) plan to invest in e-invoicing technology to create operational efficiencies.

This is followed by 'tidying' their payment process with **49%** planning to refine days outstanding on customer payments and **44%** looking to extend their payment terms on supplier payments.

FIGURE 7: Cash visibility being compromised (agree/strongly agree)
Greater levels of e-invoicing and payment automation would improve cash flow visibility for our organisation

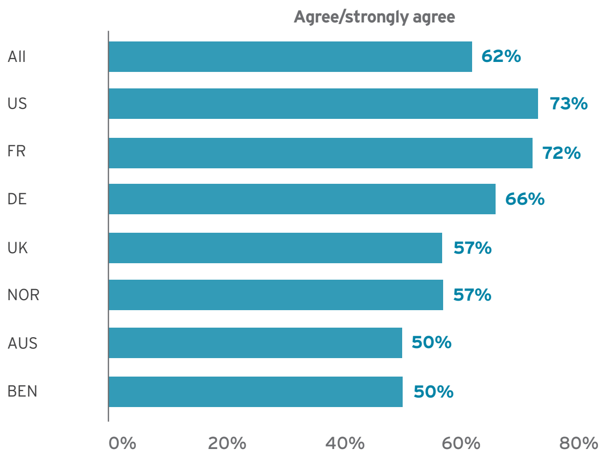
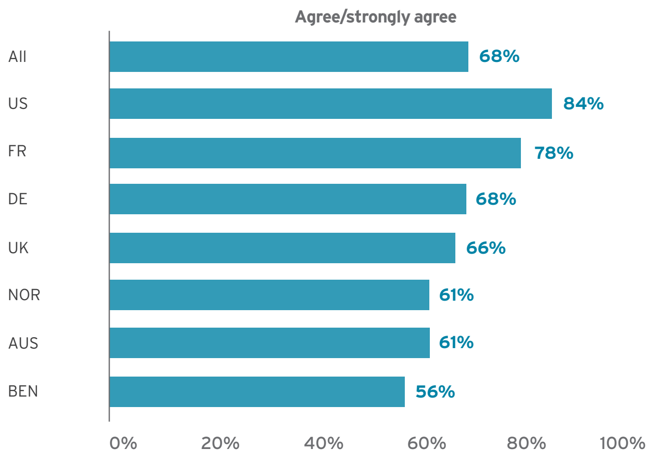


FIGURE 8: E-invoicing (agree/strongly agree)
Inefficient accounts payable practices compromise cash flow visibility



Recommendations and Summary

In uncertain times, CFO preoccupation with the cash position of the business will increase and, as shown in the data, so does the importance of cash visibility. 55% of respondents in the survey stated that it is difficult to get a detailed picture of the company cash flow position on a real-time basis.

The business critical nature of 'real-time' visibility will depend upon the business itself and it is not the case that large businesses run the financial organization 'in the dark'. However, the level of resources invested in establishing a clear picture, and the accuracy of that information are issues that will impact the bottom line. Respondents acknowledge this point when stating that inefficient accounts payable practices result in their organization having to absorb unnecessary costs (**62%**).

What challenges businesses in realising greater efficiency and visibility of cash management is the degree to which the commercial picture changes from day-to-day and the interdependency of the many systems that allow finance to run. Connecting the purchase and payment functions within the business is only one aspect of this equation yet understanding how that impacts the wider commercial landscape is critical to finance strategy overall. Changes to internal financial networks will influence compliance, cash management, supplier costs and financial planning. It appears that companies are becoming more sensitive to this issue, having learnt from past mistakes, but awareness is only part of the solution.

Organizations are now being forced to take a 'holistic' view of finance in order to control cost and cashflow more effectively. In light of the concerns highlighted around finance interconnectivity, there is a need for any new solution to be non-disruptive in its implementation and highly integrated to existing systems. However, in the networked world, integration is not only the process of knitting things together.

In order to address the concerns highlighted in this report, new solutions must account for all the processes they affect. Therefore, an e-invoicing solution must improve resource management, cash visibility, supplier connectivity and deliver cost efficiencies, but must also achieve this without the need to re-think the entire process and be flexible enough to align to existing commercial, legal, taxation and compliance needs.

Other finance implementations, large and small, must be set out with the same objectives. Disconnected payment and cash management processes will only end up compromising the efficiency and strategic value of financial operations. This is an uncertainty and compromise in a financially networked world that CFOs are keen to avoid at all costs.

Changes to internal financial networks will influence compliance, cash management, supplier costs and financial planning. It appears that companies are becoming more sensitive to this issue, having learnt from past mistakes, but awareness is only part of the solution.

Cost of Control: ‘Fuzzy Finance’

Research Report

November 2011

Basware Corporation
Linnoitustie 2, Building Cello
P.O. Box 97
FIN-02601 Espoo, Finland
Tel. +358 9 879 171
Fax +358 209 3410 244

www.basware.com