WHITE PAPER • SEPTEMBER 2017

ca technologies

Modern Financial Management—More Benefits, Fewer Spreadsheets

Financial management is the heart of project delivery, so why do so many people get it wrong?

Andy Jordan
CA Project & Portfolio Management

Organizations Execute Projects to Achieve a Financial Return

Sure, there are some projects that have to be done for regulatory reasons, and there will be a small percentage of initiatives that fall into the speculative category, but sooner or later the projects an organization delivers have to generate a return on investment (ROI). That may be a direct return (reducing costs through automation or streamlining), or it may be an indirect return (increasing customer retention and market penetration with a new product that in turn increases revenue). Of course, it's not always possible to quantify the specific return on every individual project, but to remain successful, an organization must ensure the overall enterprise portfolio is generating a return on investment—and that return must be measured.

The Lack of Transparency

When projects are being planned, financial considerations are one of the main driving forces. The organization establishes a budget for investment in projects during the next period and sets the expected ROI that investment needs to generate. Business cases are developed and projects approved based on the funds available and the extent of contribution (direct or indirect) to ROI they will make. From that point forward, the ability to achieve the required performance from a project is directly associated with the ability to control costs and retain the contribution to benefits. The problem for many organizations is that there simply isn't a framework for that management to occur.

From a benefit expectation standpoint, the business case is frequently based on hope and speculation, and that results in very little motivation to track and monitor actual benefit performance, because the baseline that is expected is little more than a sales pitch designed to get the project approved. I have some sympathy for this position on many projects. There are so many variables involved in achieving benefits that the claims and forecasts produced before work has even begun are going to have a high margin for error. However, that does mean it is even more important to keep costs under control—because that's an area organizations should be able to manage.

However, once project work is underway, the ability to track progress against budget is frequently a subjective interpretation of other factors. That may be the amount of time and/or effort that is being expended on a task compared with how much time and effort it was expected to take, or it may simply be a project manager's forecast of whether the work will be finished on time with the people assigned to that work. Neither of these approaches provides the transparency required to manage costs and ensure ROI is still on target to be met, yet many organizations have no other approach.

In today's project delivery environment, this is even more problematic than before. Planning windows are getting smaller and the rate of change is increasing as organizations seek to embrace business agility. Executives are seeking to create project environments where teams can pivot rapidly to respond to changing customer needs, to threats and opportunities identified in the operating environment and to new technological possibilities. For that to happen effectively, the organization must be able to understand which work elements are underperforming, which opportunities offer greater returns and how much it will cost to make adjustments. Those decisions must occur quickly and they must occur decisively, and without accurate and complete financial information, that cannot happen.

Attempts to Create Transparency

Today's project portfolios represent investments of potentially hundreds of millions of dollars, and there is increasing recognition that there must be transparency into those investments in the same way as there is in any operational area of the business. This results in financial managers, or the project managers who are providing data to those financial managers, trying to create accurate and complete financial cost summaries from the data they have available to them. Commonly this is nothing more than time sheets or effort summaries manually pasted into spreadsheets with generic hourly or daily rates assigned to them. Rarely do such attempts capture all of the cost considerations for a project, and even less often will the numbers be accurate estimations of actual costs. And they will likely be calculated using out-of-date numbers.

For project managers, the tracking of financial information simply isn't a priority. It isn't a measure they are directly held accountable for, and it is frequently a measure that is beyond their consideration entirely—they will typically operate on a time and effort basis in which they aren't expected to consider the cost of that effort or any other associated costs. For financial managers, unless they are embedded in the project (which doesn't make sense for most projects), they simply aren't close enough to the information to know what is accurate, what is inaccurate and what is out-of-date. Yet in this environment, organizations are still expected to make crucial financial decisions about the state of their investments and their ability to achieve the expected ROI—in fact, the ability to manage investments is critical.

As Gartner notes, "The investment view divides both operating expenditure (opex) and capital expenditure (capex) into a view that distinguishes the amount of money (and potential value) spent on investing in new capabilities from the amount spent simply running the business."[1] It is this money, and particularly value, that will drive the financial decisions the organization makes, yet it is a perspective few organizations have provided.

Creating Visibility With PPM has Historically Been Difficult

Project delivery is becoming an even faster-paced environment. Organizations are being faced with the need to make more adjustments more quickly than ever before, and to absorb those changes with minimal disruption. For that to occur, there needs to be a complete and current view of all project information, and when it comes to ensuring the right decisions are made, no information is more important than financial performance.

To ensure financial information is complete, accurate and timely, it must be sourced directly from the organization's project portfolio management (PPM) tool suite, and in turn that software must support the ability to analyze that data easily and in ways that are relevant to the business. Historically this has been a problem on both of those fronts—data capture and data analysis. From a data capture standpoint, the problems have been numerous:

- Incomplete financial data. Many organizations have focused only on time tracking—the monitoring of hours or days spent on work. This makes the translation to financial tracking more difficult, as it relies on standard rate tariffs or assumed costs, which are frequently inaccurate. While PPM solutions have long supported financial data capture, the tools have been structured around time, and financial information has been deprioritized as "non-core."
- A focus on operational costs. Because PPM solutions have tended to focus on bottom-up task planning, capital expenditures are often not even captured, as they do not directly align with those tasks. Where they are captured there has been little alignment between capital expenditure and project tasks, leaving considerable uncertainty and almost forcing capital management outside of project information.
- Inaccurate and outdated updates. The reliance on manual updates to plans maintained in PPM solutions results in data across the project that is in varying stages of currency, completeness and accuracy. Even if costs are directly captured, ignoring the problems of the first bullet point above, this will provide a confusing and misleading picture of the financial costs associated with the project.

The situation is little better from an analysis standpoint, as historically PPM solutions have contained little in the way of analysis capability. The focus is on building a time-based plan at the start of a project and then monitoring progress against that plan during the execution phase. While variances from the plan can be reported on, the ability to assess those variances is limited, especially from a financial standpoint.

This is what has led to the proliferation of manual, cut-and-paste solutions in Microsoft Excel® and similar applications to try to identify trends and forecast financial problems outside of the PPM tool. With all of the challenges identified around data capture above, this has proved challenging for organizations, and it is made worse by the fact that the analysis is often conducted by individuals removed from the project execution process. Of course, the use of manual methods to transfer data between applications will also inevitably lead to errors that may not be recognized until after critical business decisions have been made.

The Implications of Incomplete Data

This absence of financial insight is more than an inconvenience; it has real financial implications for an organization's ability to deliver results. We noted earlier that organizations conduct projects to achieve financial goals, and if there isn't timely and complete insight into whether those goals are being met, the organization is setting itself up for failure. It is inevitable that projects will experience change, either because of what has been happening inside the project or because of environmental factors impacting it. With the need for increased business agility and the shift away from individual projects toward an integrated portfolio, those changes are increasing, and every decision made without full visibility into the financial implications risks moving the organization further away from its goals.

At best, the lack of insight organizations have historically been faced with forces them to increase their reliance on interpretation of the situation—relying on stakeholders to identify what they believe to be the best decision based on an overall "feel" for the project rather than hard facts. Those stakeholders in turn rely on what they know and understand of the project in providing their recommendations, which inevitably leads to decisions that reflect their personal bias combined with the time-related information that is available to them. While financial managers may have reservations about those recommendations, they lack the information required to support an opposing viewpoint.

Inevitably this results in margins that are lower than they could (or should) be and a return on investment that is less than optimal. Perhaps worst of all, because this has been the situation for many years, the organization may not even realize how much opportunity it is leaving on the table; an ROI of 8 percent may be viewed as meeting target because there is no awareness that better financial management could consistently yield a 12 percent return.

The Solution: Accessible Financial Information, Easy Analysis

There is no reason for this situation to persist. Modern PPM solutions are more than simple project tracking tools; they offer sophisticated investment management, and that includes financial management, including analysis. Organizations need only:

1. Populate and maintain financial data at an appropriate level to allow for effective tracking and management.
2. Manage that data in ways that are relevant to the business, not just to the project.

The first of those is the simpler, so let's start there.

Business cases are necessarily conducted based on high-level estimates, but that doesn't mean financial plans cannot be refined after the project is approved. Organizations must ensure that detailed financial plans are developed alongside detailed schedule-based plans, with each work item having a financial element tied to it. This financial work breakdown should be supplemented by identification and capture of fixed costs, indirect costs and capital expenditure. All of these contribute to the overall financial picture.

It is not realistic to expect most project managers to develop this level of detail; it requires a degree of financial understanding that is not generally considered critical to the role. However, there will be no shortage of members of the finance team who can support this level of planning, and by engaging that corporate function, the organization can help ensure consistency in the data capture process—a critical part of ensuring that analysis can occur effectively.

Only once the financial plan baseline has been captured completely can we begin to think about reporting and, more important, managing that data. Here, not all PPM solutions are created equal. Effective management requires a PPM solution that can provide all of the following:

- Immediate access to summary and detail-level information
- Comparison of actual data to planned data and current forecasts (projections)
- Easily accessible interface
- The ability to leverage the information (collaboration, business intelligence (BI)-driven analytics, etc.)

The cornerstone has to be the first of these: access to the data. While virtually all solutions will allow for data entry and will capture information on actual spend as part of project updates, not all PPM suites make it easy to access that information. Effective financial management requires the ability to see spend by any number of different perspectives—general ledger account, project phase, work area, etc. It also requires the ability to drill down into any summary number to see the components of spend that make up that data and begin the process of investigating anomalies.

Of course, that investigation requires the ability to compare what has occurred with what is expected to have occurred—comparison of actual against plan—but then to also consider what has been achieved for the spend and what the implications are—actual against forecast. Effective financial management must also allow for transition between and across those elements easily and logically, and in this regard the Excel-like interface has a number of advantages; there is a reason why it is the foundation of so many financial tools and templates. However, world-class financial management functionality within PPM should provide that Excel-like look and feel from within the application interface, complete with the ability to filter, pivot and display as the user requires. If the functionality is not intuitive for a financial user, it will not be used, and the analysis will shift back to manual exports to spreadsheets.

It is difficult to overstate the importance of the ability to conduct this timely and complete analysis of financial performance. In particular, analysis of actual and planned spend to forecast, in particular estimate to completion or ETC, provides guidance to the steps that must be taken to bring a project back into compliance with the budgetary restrictions that were imposed when the project was approved. We noted earlier that benefit forecasts can be difficult to rely on, and that makes it even more important that any variance on the cost side of the ledger is below a previously determined threshold. ETC provides the clearest indication of whether that is currently the case and is the "early warning" indicator of problems.

Financial analysis can also be used to identify a situation that occurs more commonly than expected—underspending. This is not usually a problem where too much money has been assigned to an initiative, but rather where resources have been diverted elsewhere, and the underspend against plan is an early-warning sign of upcoming delays in the project. This is more than just a time issue; the required forecast spend to recover the delay may have significant impacts on organizational cash flow.

By capturing this level of financial information within the PPM tool, and in particular within the relational data model that sits behind the tool, the ability to include financial information in BI tool integration will allow for advanced analytics to be applied to financial data. This will allow for more accurate projections and forecasts, will support "what if" analysis and will provide powerful decision support when change is required.

Conclusions

It is ironic that the cornerstone of why projects are undertaken—financial performance—is so badly managed in many organizations. The focus on time-based project tracking and forecasting has become so prevalent that many organizations don't even attempt to capture a cost baseline, which creates a severe handicap when trying to make business-focused decisions during project execution. That is simply not a sustainable model in today's business-agility-driven world, and organizations must immediately ensure that they are addressing this with all of the following steps:

- Undertaking comprehensive financial planning to the same degree of precision as time-based planning
- Considering capital and operational expenses, hard and soft dollars, direct and indirect costs, etc., to ensure that a complete picture of the project financials are captured as part of the planning baseline
- Integrating finance department resources into the project management and tracking process to provide the required level of expertise to capture and manage financial information
- Actively managing financial performance to the same degree that other constraints are managed, with a focus on maintaining and improving financial performance in an evolving project delivery environment
- Leveraging a solution for their PPM needs that supports this best practice approach to financial management and doesn't force compromise on analysis or decision making

The old adage is that we manage what we measure. If we aren't measuring financial information properly, how can we hope to manage our investments effectively?

To learn more about how CA Project & Portfolio Management supports financial management, visit **ca.com/PPM**

Connect with CA Technologies

CA Technologies (NASDAQ: CA) creates software that fuels transformation for companies and enables them to seize the opportunities of the application economy. Software is at the heart of every business, in every industry. From planning to development to management and security, CA is working with companies worldwide to change the way we live, transact and communicate—across mobile, private and public cloud, distributed and mainframe environments. Learn more at **ca.com**.

1 Jim McGittigan and Cesar L. Lozada, Gartner Inc., "Run IT as a Business Using Six Pillars of IT Financial Transparency to Drive Value," May 31, 2017

ca technologies

CS200-303073_0917