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Beyond information to insight: the promise of management reporting

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Information Management

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Too much information can paralyze executives and managers just as severely to as too little information. Sure, you can easily find out how many paper clips are on hand, but will that really help you run the company? Probably not.

This is the fifth in a series of six articles seeking to establish a new agenda for finance. In the first, David Axson and Greg Hackett make a case for change, providing a wake-up call to today's finance leaders, and the second describes the new vision in greater detail. The third article discusses transforming the planning process to make it simple, flexible, short, and relevant to today's dynamic business environment. The fourth article addresses the rapidly emerging role that finance is being asked to take on – that of risk manager. In this, the fifth article, David Axson explores the often vexing issue of delivering insightful, focused, and timely management information that supports better, faster decision making.

David Axson is an advisor to the IBM Cognos® Innovation Center for Performance Management. He is an unflinching advocate for innovation in business management practices, questioning the effectiveness of the status quo and urging companies toward better ways of doing business.

The final article in the series will elaborate on the actions managers should take to get started on this new journey and also describe an implementation road map. Read on to learn how you can transform financial and operational reporting processes at your company.

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Time to end the disappointment

In 1963, Business Week commented that, "The great day—when all the information for solving a management problem is only a push button away—is closer than you think." Well—more than forty years later we are still waiting!

The last 20 years have been widely hailed as the Information Age and rightly so; advances in computer and communications technologies have brought an avalanche of new information sources online. Any individual with the most basic computer skills and a broadband connection can access more information from their computer than is contained in all the world's libraries combined. While initially seeming to be both empowering and liberating, for many the effect has been the exact reverse. The explosion in data, information, reports, and measures has created confusion and fear.

Managers today face the challenge not of having too little information, but too much. The explosion of business information residing in ERP systems, CRM systems, data warehouses, and the like, has in many cases had the exact opposite of the intended effect; decision-making has become slower and less confident at the very time that speed and agility are more essential than ever. Decision-making becomes hidebound by crises of confidence induced by conflicting indicators, divergent analyses, an inability to isolate the critical from the merely interesting, and a realization that the results of any decision will be instantly available to superiors, peers, and competitors. Without radical action, companies will continue to find themselves blindsided by major trends—both inside and outside their organizations—that avoid detection amongst the forest of data.

Less is more

Leading companies recognize the problem and are embarking upon radical programs to assure that their performance reporting and analysis equips managers to respond to the volatilities and complexities of today's markets. The changes are based on an understanding of six new rules governing a company's performance reporting and analysis.

1. Information needs are finite

2. Focus on ratios, not absolutes

3. Favor breadth over depth of content

4. Deliver insight, not just information

5. Just in time, not just in case

6. Balance needs to reflect reality

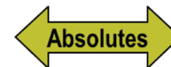
First recognize that business information needs are finite. Not everything that can be reported needs to be reported. There is a known universe of measures of importance based around markets, customers, operations, employees, suppliers, competitors, infrastructure, projects, compliance, risk, and financial results. Such measures provide a comprehensive framework for defining the key relationships and ratios that allow managers to understand performance and rapidly respond to opportunities and threats. Companies should be more selective regarding performance measures. There has been a tendency to seek quantitative measurement and reporting of everything. More useful is to separate the frequency of measurement from the frequency of reporting. By all means, continuously monitor many aspects of the business, both internally and externally, using automated tracking systems, but only report such measures when they matter. This is accomplished by triggering reporting based upon exceptions to predefined tolerances and exceptions adjusted for materiality so that only relevant information is reported.

Second, abandon the reliance on absolutes. Recognize that a single data point cannot be a key performance indicator. Ratios are the solution; measure linkages, relationships, interdependencies and trends (See Exhibit 1). Instead of focusing on key performance measures, think of key performance ratios. Define the critical business ratios—typically no more than 20— for the corporation. Examples could include revenue growth relative to the growth of the market or the relationship between changes in customer satisfaction and revenue per customer. These ratios will vary by company based upon the type of business, the company's organizational structure, the external environment, the life-cycle stage of each line of business (See Exhibit 2), and the chosen management model. Cascading these ratios throughout the organization helps ensure alignment and accountability. Each manager should focus on no more than ten key ratios, about 30 percent of which should reflect external or market-based factors. Standard time-based reporting should be eliminated, shifting to reporting triggered by events, trends, or tolerances.

Exhibit 1: Measure relationships, not absolutes

Quotes for new products

22



Sales this month

$42 million

New customer quote activity

$$\frac{\text{\# of quotes for new products} + \text{\# of quotes for existing products}}{\text{\# of quotes for new products to new customers} + \text{\# of quotes for new products to existing customers}}$$

Sales trend index

$$\frac{\text{Sales this month}}{\text{Customers sold this month}} \times \frac{\text{Total customers sold}}{\text{Cumulative sales to date}}$$

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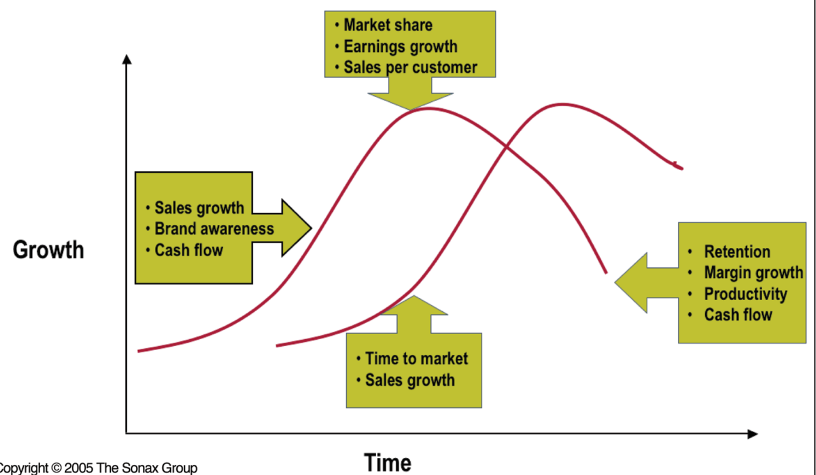
Perhaps the most widely cited requirement of a company's management information systems is for the ability to "drill down" from an aggregate measure to progressively lower levels of granularity. While in some cases more detail may equate to more insight, it can more often lead to increased confusion as successive levels of drill-down exponentially expand the set of information to be analyzed. Many now understand that drill-down has its place and is not a silver bullet. In many situations, managers recognize that more breadth of information offers much greater support to effective decision- making than does greater depth. Consider the relative value of drilling down on travel expenses to incremental detail of specific expense types such as airfare, meals, and lodging compared to offering greater perspective on the reasons expenses were incurred, such as those triggered by customer service problems versus those incurred as a result of prospecting for new business. The third rule is to favor breadth of information over depth. Providing the context to show how individual functions, actions, or activities relate to each other is more valuable than delivering progressively more detail on a single item.



The fourth rule is to focus on delivering insight, as opposed to simply providing information. Insight comes when all analysis answers three questions:

1. What happened?

2. Why did it happen?

3. What alternative courses of action exist?

Most reports do a decent job at answering the first question; some will provide analysis as to the causes of the situation being reported. However, for real insight that equips the recipient to make better, faster decisions, management information should offer guidance as to the levers that are available to respond to the event being reported. Insightful management information goes far beyond simply reporting events by describing what happened or may happen, current or potential impacts, the reasons behind the trend or event and—most important of all—guidance as to the options available to management.

"Just in time" has been the mantra for supply chain professionals for years, but for finance professionals, "just in case" might be a better descriptor. A tendency to have all possible information available just in case it may be required has contributed to the overload of information. In many ways, technology has fueled the situation through the provision of ever more mechanisms for the storage and dissemination of information. It has become all too easy to add information and reporting capability. Unfortunately, less progress has been made toward taking advantage of technology's ability to select, filter, and synthesize data based upon specific criteria and logic, so that only actionable data is reviewed. Reporting should be driven by the data that is needed, not simply what can be obtained from systems.

The power of current CPM tools makes the ability to deliver precisely the right information – not too much and not too little – to the right people at precisely the right time to maximize the probability of making the most informed decision possible a realistic objective. Building appropriate logic into reporting tools can fulfill the promise of "just-in-time reporting" that is tailored not only to the recipient, but also to the situation at any given time. For example, the information needs of managers are very different when engaged in completing staff performance reviews than when assessing the viability of a new capital investment program. The ability to structure reporting around the rhythm of the business rather than the calendar and around the roles of the recipient greatly enhances the potential for timely, insightful decision making.

The final rule is to ensure that an organization's management information has an appropriate balance. In this area, the Balanced Scorecard has proved a valuable addition to the tools companies use. But many organizations have found that the balance implied between the four dimensions of financial, customer, business process, and learning and growth is more intention than reality. To many, a more rational approach is to adopt a different view of balance that looks at the relative mix of leading and lagging information and internal and external information. (See Exhibit 3). Today at the average company, over 70 percent of information available to management is internal and historic in nature, sourced from transaction systems that diligently record all the organization's activity, but offer neither context as to what is happening in the marketplace nor insights into future trends. A more appropriate balance combines internal, lagging information with more useful external, leading, or predictive information that allows managers current performance with likely future threats and opportunities. Technology can play a key role in enabling this change. Finance should leverage vehicles for capturing, organizing, and "Googlizing" unstructured data and integrating it into the reporting processes.

Getting started – testing the value of current management information

Astute organizations are taking time to fundamentally reassess their performance reporting and analysis capabilities in the light of the increasingly volatile and uncertain external markets and the untapped potential of technology to move beyond simply automating current reporting to delivering selective, focused, timely, and insightful analysis to support better management decision-making. A start on that journey is to test all management reporting against seven measures of reporting value (see Exhibit 4). First, the information must be relevant to both the business and the recipient. This can be answered with a two-part question, "So what?" and "Who cares?" Answering the former establishes whether the information matters, while the latter establishes responsibility and ownership. Second, reporting must establish the trend for the measure being reported, in essence answering the question, "Is the trend getting better or worse?"

Exhibit 3
Redefine balance

Target for balanced performance reporting

	Lagging	Leading
External	20%	20%
Internal	30%	30%

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Third is a test of materiality. For each key business ratio, the organization must establish a tolerance or range that defines the boundaries or limits of acceptable performance. Traditionally, this has been a plan or budget number which rapidly became irrelevant, but today companies are increasingly using much more dynamic, market-based measures to establish relevant tolerances. Having established an acceptable range for the ratio, the reporting logic can be defined to provide first an early alert that this ratio is approaching the limit of acceptability, and then a call to action as the threshold is breached.

Exhibit 4:
Test the value of current performance reporting

Required Attributes
1. Relevant ratio
2. Trend
3. Tolerance
4. Early alert
5. Call to action
6. Forecast impact
7. Additional information for context

Close ratio
Orders placed / Quotes issued
70%
60%
50%
40%
30%
20%
10%
0%
J F M A M J J A S O N D
Watch
Warning
• Pipeline of quotes has dropped 30% in last 30 days
• ABC Inc is aggressively discounting in top 20 markets

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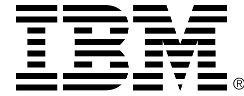
The last two elements of a high-value report are a forecast or projection of the ratio's future trend or value based upon current information, and the addition of contextual information that assists the recipient in narrowing the range of potential actions. Taken together, these seven attributes ensure that reports maximize the probability of timely, decisive, and appropriate decision-making.

Summary

The combination of a turbulent world and increasingly short cycle times in which to make decisions is placing intense pressure on corporate planning and management information processes. A key step is to align management information and analysis processes with the decision-making cycles of the business. This demands a move away from exhaustive, calendar-based, primarily internal and finance-focused reporting supported by largely ad hoc analytical processes, and toward event-triggered, situation- specific, synthesized, and insightful decision-focused information.

Through the combination of objective design, applied logic, and the power of world-class performance management technology, the potential exists to transform management reporting and analysis into a dynamic management process that enhances short-term performance and provides a platform for eliminating the burden of ineffective planning, budgeting, and forecasting discussed in our earlier papers. The new rules for best-practice performance reporting and analysis can help companies fulfill the promise Business Week foresaw four decades ago.These patterns, as well as your own business processes, are ingrained in the ways people work. Studies have shown that when corporate processes are changed, one-third of the people will embrace the changes, one-third will resist the changes, and one-third will leave the organization. You need to understand that this is a significant change in mind-set. Focus on the value of the activity—greatly reduced effort in the budgeting process.

Don't ask for excessive detail, especially at the initial roll-out. You don't need actuals—you need information for forecasting.



About the author

David Axson is a partner in The Sonax Group and an advisor to the IBM Cognos Innovation Center. He is the author of the book "Best Practices in Planning and Management Reporting" published by John Wiley. He can be contacted at daxson@sonaxgroup.com.

About the Sonax Group

The Sonax Group is a consulting and advisory firm redefining business management practices. Established by David Axson a cofounder of the renowned benchmarking and finance transformation authority The Hackett Group, the firm works with executives to improve the effectiveness of their planning, performance management, and decision-making processes, radically simplifying and refocusing them to achieve flexibility, agility, confidence, and consistency.

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