UNLEASHING FP&A

A Primer on Financial Planning & Analysis (FP&A) and The New Solution for Small & Midsize Businesses (SMBs)

MANAGED FP&A SOLUTIONS

FIRSTWATER

RELATIONAL FINANCE PARTNERS

INTRODUCTION

Whether you're just getting started with financial planning and analysis (FP&A) in your business, or have a dedicated team, this whitepaper is presented to ignite or fan the flames of your finance dialogue.

Specifically, we will cover:

- ✓ What is FP&A, the core capabilities, and the benefits of investing in FP&A for your business
- ✓ A comparison of larger company finance organizations to small and midsize businesses (SMBs), including team costs
- ✓ Software trends in reporting and visualization platforms, and the problem of optionality for SMBs
- ✓ The new solution for SMBs to unleash FP&A in their teams and companies, Managed FP&A Solutions (MFS)

> *The best way to get big is to act big, and by investing in finance capabilities earlier businesses can reach their goals faster and with less risk.*

THOUGHT LEADERSHIP BY FIRST WATER

First Water connects teams with data and companies with capital through Relational Finance.

With experience spanning private equity, investment banking, commercial lending, FP&A, and SMB leadership, First Water draws from different skill sets and perspectives to accelerate growth, reduce risk, attract capital, and maximize the value of businesses.

First Water has eliminated traditional SMB barriers to finance capabilities through the creation of the Relational Finance model. Partner companies get tailored access to financial planning and analysis (FP&A) and corporate finance expertise without the rigid engagement frameworks or upfront transaction requirements of legacy models.

Finance innovation is at the heart of our mission, including the development of thought leadership and educational collateral via books, whitepapers, blogs, and newsletters. Thank you for taking the time to join in our dialogue.

Learn more at www.firstwateradvisors.com.

WHAT IS FP&A

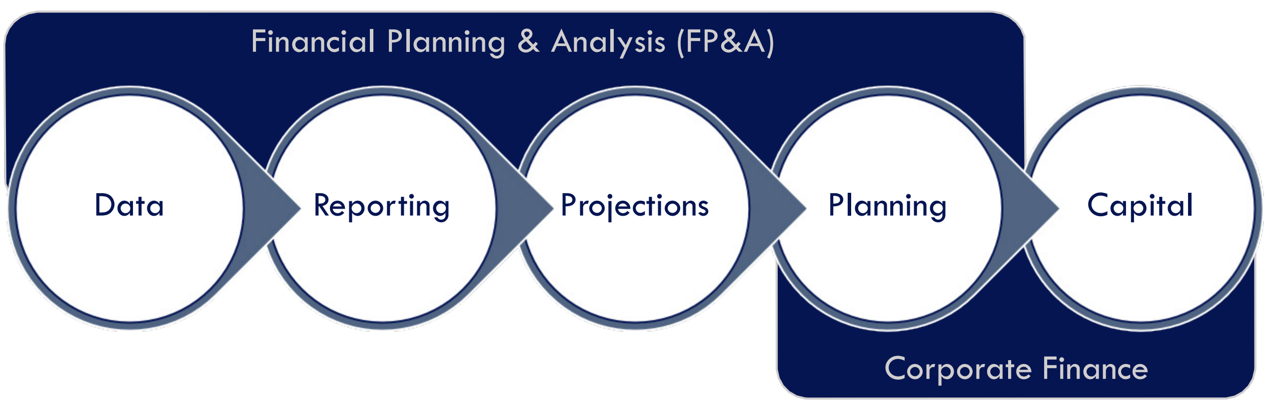
Financial planning and analysis, or "FP&A", is a critical component of the finance function of a company. Sometimes referred to as "operational finance", FP&A is the data hub and processing center of an organization. FP&A is where operational information (production, asset utilization, workforce planning, etc.) is married to financial information (revenue, expense, AR, etc.) to create a complete picture of the business and provide leaders with context for critical decisions. The quality of an organization's FP&A translates directly to its financial performance and outcomes.

The moniker of operational finance orients FP&A as the part of the finance function tied to operations and the drivers of profit and loss (the income statement). Although the 'F' in FP&A stands for 'financial', it is important to highlight that financial data is not the only relevant data. FP&A is most valuable when it establishes the connection between operational activities and financial performance.

The finance function counterpart to FP&A is corporate finance, which deals with sources of funding, the capital structure of the company (the balance sheet), and investment decisions. Larger companies also segment treasury (cash management) from FP&A and corporate finance.

In *Relational Finance*, the book by First Water founder and CEO Ben Lehrer, the finance function is summarized as five pieces which themselves make up a "finance spectrum" of related capabilities. By thinking of these as sequential and interrelated, we can see which pieces apply to FP&A and corporate finance, where they overlap, and why FP&A serves as a foundation for strong corporate finance. We will dig deeper into the day to day responsibilities of the FP&A team and the benefits created.

The Finance Spectrum



> *FP&A serves as a foundation for strong corporate finance execution.*

Reporting & Business Intelligence (BI)

The FP&A team is responsible for dissecting financial and operational data to analyze and visualize the how and the why of performance. This analysis is used to support internal dialogues in reviewing results, tracking against goals, and digging into the root causes of any variances versus expectations.

When done well, the *right* data drives the *right* conversations. When done poorly, leadership doesn't know what to focus on and may be buried under reams and reams of paper, also known as "reporting hell". No one sets out to end up in reporting hell, but it can easily develop over time as managers institutionalize one-off data requests without regard to how insightful or actionable the information is on an ongoing basis. "Reporting for reporting's sake" does not make for a good FP&A function.

Benefit 1: Higher Team Accountability

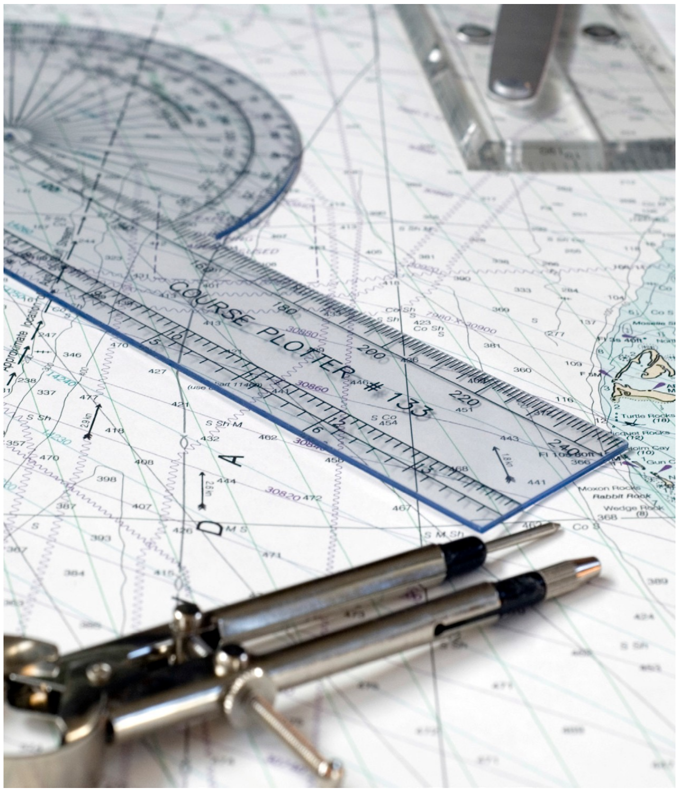
You can't manage what you can't measure. Goals that aren't specific, clearly communicated, viewed as achievable, or clearly tracked against lead to finger pointing. Quantifiable targets aren't the only thing that matter in motivating and assessing your team, but they are a key part of the equation when increased growth, productivity, efficiency, and profitability are part of the company's goals. Accountability applies to leadership as well. Goals which aren't operationally achievable or can't be delivered on financially can kill morale, or worse.

Budgeting, Forecasting & Scenario Analysis

In order to set goals and plot the path forward, the FP&A team is responsible for building credible views of the future, **translating inputs for operational drivers into financial outcomes** (income and cash). These tools and processes are used to plan for hiring needs, financing requirements, and to communicate the financial narrative to the stakeholders whose interests are tied into the outlook (leadership, board, lenders, investors, potential partners, etc.).

Budgets and forecasts are often obsolete once they are posted, as new performance data and other information becomes available. FP&A is also responsible for testing different outcomes, understanding the impact on cash and key financial metrics. This is critical in managing risk and getting ahead of necessary conversations when things don't go according to plan. This is equally important for positive events as it is for negative surprises!

For example, when launching a new product or service, the FP&A team should evaluate and size a range of outcomes from raging success (requiring additional equipment, people, and supplies) to an absolute failure (shut down and cost reductions). Scenario analysis is a powerful tool and can **save a business from placing a bet it can't afford to lose**.



Benefit 2: Improved Business Visibility

Decipherability and project-ability are powerful things, offering **visibility and insight** into what has already happened and what may happen in the future. It is often underrated how solid reporting impacts your ability to forecast; the better you understand how the pieces fit together, the more scientific your projection build-up.

By reporting along the same metrics and drivers by which you forecast, you are better able to use actual performance data to **inform future assumptions** (and test your previous assumptions against actual results). Reporting and forecasting create a positive feedback loop so that both get better over time.

Capital Allocation Support

When there are more opportunities at hand than there is capital to allocate – hopefully this is the case more often than not – the FP&A team is called upon to develop the frameworks to assess potential return on investment (ROI) and related risks. Best practices call for "capital allocation methodologies" which include thorough analysis, return hurdles, and approval processes. FP&A brings structure and process to where capital is invested and how it is prioritized.

Benefit 3: Confident Decision-Making

Analysis and project-ability are the foundations for **confident and informed decisions**. Knowing the amount of breathing room you have if you swing and miss is critical before you step into the box. When choosing between several options, the capital allocation process helps you assess and **prioritize investment** of your resources. Plus, if you are betting the farm, it is helpful to know that when you are pushing the chips to the middle of the table.

Transaction Support

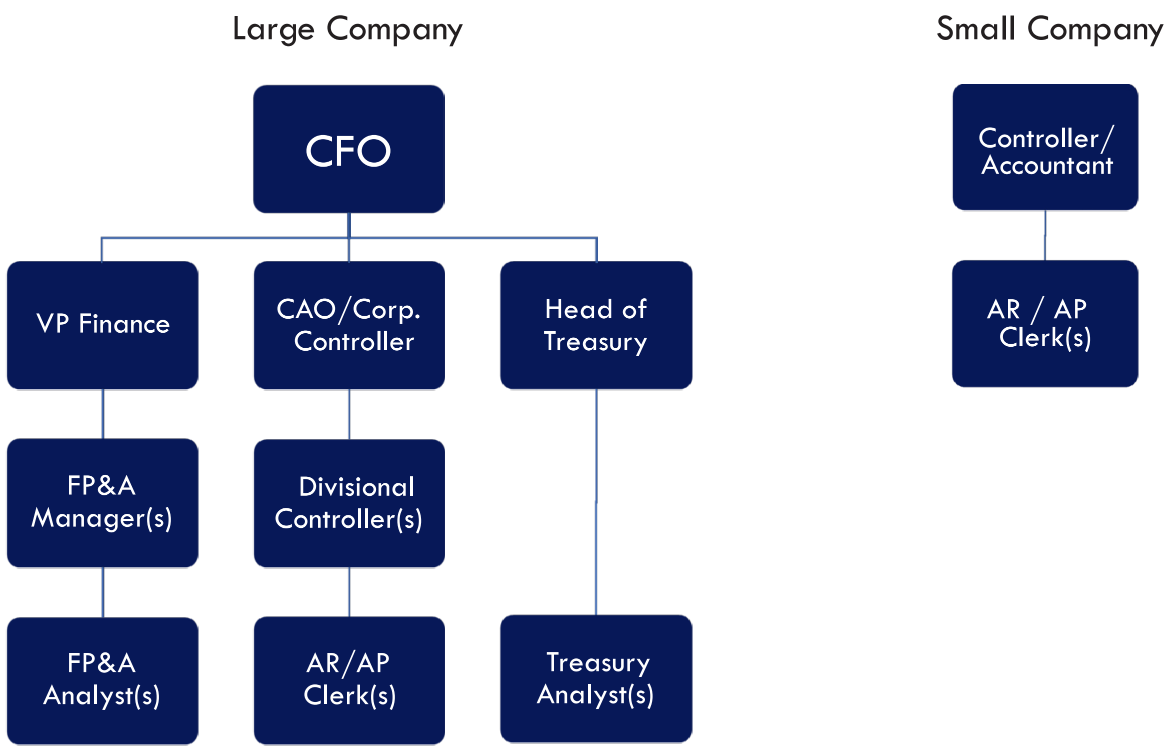
Whether buying, selling, merging, partnering, or pursuing a debt or equity capital infusion, the FP&A team is called upon to provide analyses, projections, and due diligence information. FP&A fills a critical role in any situation where financial or other data analysis is required. Larger, acquisition-minded companies sometimes break this out into its own function called "corporate development" which combines portions of FP&A with strategy development and transaction execution.

Benefit 4: Tailored, Data-Driven Storytelling

With data at your fingertips and a credible roadmap for the future, you have the foundation for telling the best story about the outlook for your business. Whether you are rallying the troops, requesting more credit from your bank, raising money from investors, considering a merger or acquisition, or selling your business, FP&A plays a critical role in **crafting the *right* story** that addresses hot button issues specific to your audience. Also, and equally important, the availability of data and presence of FP&A processes add a lot of **credibility** to the storyteller.

BIG VS. SMALL COMPANIES – THE FP&A DIFFERENCE

When it comes to finance, the team organizational chart looks quite different in larger companies versus SMBs. Here is a comparative example:



Underneath a Chief Financial Officer (CFO), large companies typically have dedicated teams for FP&A, Accounting, and Treasury (as well as Corporate Development, depending on the organization). These may not be the only things the CFO is responsible for, such as Legal or IT, though they represent the core finance and accounting functions we will focus on for this discussion.

In a smaller company, these functions tend to get combined into a much smaller team out of financial necessity. Further, the experience and professional background of the functional leadership can differ dramatically. Whereas a seasoned large company CFO might have significant scar tissue in finance, accounting, treasury, legal, sales, capital raising, and/or mergers and acquisitions (M&A), the corresponding position in a smaller company tends to be accounting-focused. Many times, especially in family-run businesses, this team member has learned the position on the job with little to no prior experience.

In the org chart comparison, the FP&A piece is typically absent in smaller companies. It is not as if smaller companies would not reap the benefits from having FP&A capabilities, as better performance visibility and project-ability benefit every business. You can easily argue that smaller companies need these capabilities more as they often operate with less wiggle room and more financial constraints than their larger counterparts. So those that need the skills the most often have the least, or none at all. Why?

From our extensive work with SMBs, here are three themes we have come across related to the inability to reap the benefits that FP&A has to offer:

- ❑ **Experience Blind Spot**

  Many entrepreneurs or SMB leaders have not had exposure to the workings of a large company's finance and accounting team, especially FP&A. When starting businesses, entrepreneurs typically succeed by making, selling, or packaging something better than predecessors, not because they are finance wizards. Already wearing multiple hats and moving quickly, it can be difficult to step back and find the time to get schooled up on finance capabilities.

- ❑ **Mission Critical Priorities**

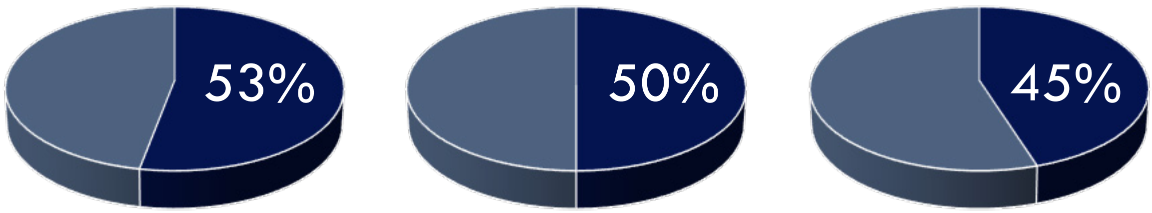
  Accounting and treasury have been traditionally viewed or mandated as mission critical. You have to manage your cash, invoice your customers, pay your bills, and give your bank the information they require to extend credit. No doubt these are critical elements, though they aren't the only ones. Since the accounting and treasury need often starts from Day 1, SMBs add these people first resulting in a conflation of finance with accounting.

- ❑ **Limited Financial Resources**

  Employees, systems, and additional resources require investments, and capital can be scarce in smaller companies. Of all the opportunities to invest, FP&A has historically lagged in garnering priority compared to investments with more immediately tangible impact on sales or production (like hiring another salesperson or adding another delivery truck). This makes sense, until it doesn't.

> *Deciding to prioritize finance is not a question of if, but when. SMBs have an opportunity to turn finance into one of their strengths. Growing a business beyond its current state and positioning as an attractive investment for capital partners depends on it.*

However, even larger companies struggle with FP&A. As part of a 2018 *Berkeley Research Group* survey of over 100 senior finance executives, respondents were asked for their top 3 challenges in accomplishing their finance priorities. The following were prevalent in responses (ranked in the top 3 challenges faced):



Too many fire drills or inefficient processes

Understaffed or lacking management capabilities

Insufficient tools or data issues

For SMBs, these topics are particularly relatable. With limited or no direct finance staff, SMBs simply lack the horsepower to turn on FP&A capabilities without significant investments.

THE TRADITIONAL FP&A STACK

So how much does FP&A cost? As a starting point we can look at the FP&A team structure in that larger company. Roles, responsibilities, and costs are tiered, hence the term "FP&A Stack".

Chief Financial Officer *$400k+*

- Strategic Business Leader for Value Creation
- Finance, Accounting, and Treasury Oversight
- Board, Capital, Investor Relationship Management

Vice President Finance *$200k+*

- Finance Function Oversight
- Process Design and Leadership for Reporting, Budgeting, Forecasting
- Project Management

FP&A Manager(s) *$125k+*

- Reporting, Budgeting, Forecasting Process Management
- Financial Model Development & Ownership

FP&A Analyst(s) *$75k+*

- Reporting, Budgeting, Forecasting Support
- Ad-Hoc Analysis

Full Cost of FP&A Stack (w/2 Managers, 2 Analysts) = ***$1m+***

Team structure and cost by role vary widely across companies of different sizes and types, but in this example two things stand out.

First, the FP&A Stack requires multiple skill and experience levels in order to open up the full capability set, which goes beyond analysis to include process design, project management, stakeholder communication, and driving value creation. That's a lot of skill sets!

Second, the cost of this team can be substantial, well in excess of $1 million per year. Senior finance professionals are highly-compensated, and generally there is a smaller pool of available talent versus accounting. This is partially due to the long-standing trend of companies not investing in finance as early or often as areas like accounting. Plus, FP&A is not prevalent in higher education curriculums compared to accounting and corporate finance – this needs to change!

Smaller companies have been left in a bind. Even as top leaders embrace the value of finance and FP&A, the price of entry is substantial. You need multiple team members, and they are expensive. **There is no doubt that improving visibility, accountability, decision-making, and story-telling can help you accelerate growth, reduce risk, and create more value in your business.** The challenge is in stepping back from day to day operational needs (the "day job") to recognize and develop the benefits of FP&A.

By making FP&A investments, companies get a leg up on the competition with differentiated capabilities. In an increasingly competitive world, can you afford to pass up any opportunity for an advantage?

SOFTWARE TRENDS AND THE PROBLEM WITH OPTIONALITY

Many new reporting tools and systems have come to market over the last decade. On the surface, having more options at better price points seems wonderful. However, the multitude of offerings also poses a challenge to business leaders who hope to pick the right pieces to work together and meet their needs now and in the future.

If you lock into the wrong platform, you can set yourself back in a big way when you outgrow the system, it doesn't integrate with other critical pieces, or you lose/lack the internal resources to manage the processes. What was originally thought of as easy and affordable can very quickly become cinderblocks around the ankles of the company.

Here is a sample of the types of systems and tools that are available. You may be familiar with some of these, but it is by no means an exhaustive list. We're not endorsing one over any other here, simply showing how many choices there are out there today. Note there is significant vendor overlap between categories, as an individual provider may have Accounting, ERP, and Business Intelligence (BI) solutions under one or more brand names.

ACCOUNTING	ENTERPRISE RESOURCE PLANNING (ERP)	BUSINESS INTELLIGENCE (BI)
• QuickBooks • Microsoft Dynamics • Sage 50 (Peachtree) • Intacct • Xero • Multiview	• NetSuite • Peoplesoft • Workday / Adaptive • Epicor • Infor Syteline • SAP	• Power BI • Tableau • Domo • Qlik • Host Analytics • Sisense
G2 Crowd – Accounting Software	G2 Crowd – ERP Software	G2 Crowd – BI Software

With many of these systems having customized, long, and expensive implementation processes, it is not a decision to be taken lightly. Further, leaders cannot rely on a vendor salesperson to offer a truly objective view across options. Life was much simpler when it was just vanilla, chocolate, and strawberry!

With more reporting and analysis systems within reach of SMBs, it is critical for leaders to remember that no system, in itself, is FP&A. Systems only solve bottlenecks. All too often companies make a system leap too soon. In order to gain insight, leaders must first invest the time and resources necessary to identify the information that is critical to managing their teams and businesses. When such information is synthesized into the operational and financial drivers that translate into long-term value creation, only then should businesses take the plunge on significant system investments to improve controls, connectivity, and visibility. Nifty visualizations and mobile reporting platforms are not synonymous with insight.

Always keep in mind that no system will tell you how to run your business; that would be like buying a Ferrari with the expectation that the car itself will teach you to drive. A simple spreadsheet, with the right data that answers the right questions, will serve you better than an elaborate system spitting out high volumes of noise.

INTRODUCTION TO FIRST WATER

First Water is the one-stop finance shop providing business leaders and owners with access to finance capabilities and expertise. With the complete finance toolbox, the flexibility of the Relational Finance model, and the diverse experience of our team, we have eliminated historical barriers to FP&A while providing SMBs with partners on their side of the table with 'other side' experience.

First Water Finance Toolbox

FIRESCORE	ROOTSOURCE	TALEWIND	LIFEBLOOD
Growth & Capital Roadmap Assessment	**Reporting & Business Intelligence (BI)**	**Planning, Budgeting & Forecasting**	**Capital Raising & Transaction Execution**
Align financing options with your growth objectives and personal goals to plot the path to success.	Gain insight into financial/operational performance, with the *right* data driving the *right* dialogue.	Build credible outlooks to set goals, test assumptions, make confident decisions, and tell your story.	Act on capital and transaction opportunities to accelerate growth or monetize the value you've created.

MANAGED FP&A SOLUTIONS (MFS)

First Water has developed an innovative solution for SMBs that enables critical elements of the FP&A Stack. Pulling from the RootSource and TaleWind components of our finance toolbox, First Water MFS offers eye-opening improvements in reporting, business intelligence, forecasting, and planning/budgeting while providing access to seasoned finance and investment professionals.

In one fell swoop, you improve business management and decision-making with increased visibility. Simultaneously, you add the value of numerous finance disciplines (private equity, investment banking, commercial lending, FP&A) into your internal dialogue. **No other service offering in the market offers this suite of capabilities and access to finance acumen, and MFS can be implemented and maintained for a fraction of the cost of the traditional team.**

Although MFS can be applied to any FP&A-related activities, the most common applications are the following:

- ❑ Three-Statement Reporting & Forecasting (Operating Model)

  First Water develops and maintains a singular data hub and tool that provides financial reporting and forecasting capabilities. The operating model is particularly useful for financial consolidation across multiple entities and disparate systems, and enable driver-based and dynamic forecasting (e.g. travel and entertainment expenses forecasted based on the trailing 3-month average spend per FTE).

- ❑ 13-Week Cash Flow

  Large companies can spend hundreds of thousands of dollars developing and implementing a detailed 13-week cash flow tool and related process. Incorporating invoicing, accounts receivable, accounts payable, general ledger, and other financial information, First Water can implement and maintain a 13-week cash flow process with customized levels of forecast granularity to help you keep tabs on your most precious resource (liquidity).

- ❑ Power BI Dashboards

  Using data from company systems as well as forecast information, First Water can implement and maintain Power BI dashboards to help management keep its finger on the pulse of performance and to drive impactful conversations and decisions.

> *"The key lies not in having better information, but in turning information into information that cannot be ignored."*
> *- Jim Collins, Good to Great*

Outside of the major benefits of these FP&A capabilities discussed previously, MFS offers additional advantages, including:

❑ Access to Finance Experts & Perspectives

We're finance people, not software people. When it comes to reporting/forecasting, we care about highlighting the right data for the right dialogues. Want to know how lenders, private equity buyers, or investors analyze your business and financial performance? With MFS you build a recurring dialogue with the First Water team, a value no software platform can offer.

❑ Continuity of FP&A Processes

If you do have dedicated finance personnel in your company, the departure of one or all of your team can be highly disruptive to processes relied upon to make decisions and run the business. MFS eliminates turnover risk while giving you a single relationship touch point built on repeatable processes.

❑ System Agnostic

MFS works with any accounting system and operational dataset format as long as it is exportable to a spreadsheet. No changes to underlying systems are required unless deemed critical to MFS accuracy or efficiency (identified during discovery).

❑ No Major Software Commitments

MFS leverages recent enhancements in the data connectivity of common platforms (Microsoft Office, QuickBooks, etc.) to semi-automate the aggregation of information. By utilizing common and affordable tools, MFS can deliver insightful FP&A with no long-term commitment or costly implementation for a new software platform. This is critical for growth companies where accounting and system needs may change over the intermediate term.

❑ Scalable with the Growth of Your Business

Whether you are launching a new business line, expanding your chart of accounts for more granularity, folding in a new acquisition, or even changing systems, MFS is flexible enough to quickly incorporate changes as opportunities arise and business needs change. Many partner companies also leverage MFS to build account structure consistency to support system planning and implementation processes.

❑ Cost Effective

Available on a monthly fee basis, MFS is accessible for a fraction of the cost of a traditional FP&A team. You get critical components of the FP&A Stack, spanning multiple roles, from a single source. Our team brings the experience of the entire FP&A Stack, because we have sat in every role!

NEXT STEPS

Contact First Water at info@firstwateradvisors.com to determine how MFS can benefit your business and accelerate you along the path to your goals.

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