Business Perspectives
Finance and Accounting Perspective

I'm the Chief Financial Officer (CFO) at 'Step' plc. Two years ago, the firm was facing big problems. Performance was poor and jobs were at risk. The Chief Executive Officer (CEO) organised a meeting with the bank manager, representatives of union, employees and local municipality to resolve the problems.

I started the meeting as follows:

'According to the financial statement produced following IAS standards, our ROS dropped from 8.5% to 5% in the last quarter. Last year ROE decreased by 34.7% and we have difficulties in finding new investments opportunities because our WACC is too high (16.5%). The bank is charging us 450 basis points on EURIBOR.'

During my explanation, the bank manager was taking a look at the provided figures and commented 'I see your point but our decision is linked to Step's financial structure. Your gearing went up by 50% and the interest cover down by 67%. We anticipate you'll have some difficulties in matching the covenants on the long-term loan as well as the repayment plan of your 2012 – 5.2% Bond. By the way, last quarter the ROS was not 5% but 2% and WACC is not 16.5% but 18.3%. We're really concerned about your capability to find investments with a positive NPV.'
As soon as the bank manager finished, the union representative said 'I'm really concerned about your calculations: please revise them since the firms' ROS is 7.5%. Having said that, I personally think employees' productivity is very good and you cannot blame them for poor performance: number of products per employee went up by 5% and the cost of personnel on the overall direct costs went down by 2%.'

The local representative argued 'Please, keep the eye on the ball: the firm is the main contractor in the area with more than 25 SMEs whose lives depend on Step. Last year the municipality financed the new link with the motorway (mainly to help Step) with an investment of €1.5mln'.

The CEO immediately interrupted the municipality representative 'yes and we appreciate it but we paid more than €25.5mln taxes only in the last year!'

An employee raised a hand and said 'I don't understand too much about IAS, WACC, ROS, EURIBOR, gearing, basis points, etc. It makes no sense to me. Could you explain me what the problem is?'

The CEO immediately gave his explanation 'the cost of debt is too high' but the bank manager returned 'you're wrong, the problem is not the cost of debt but the increased gearing and the poor productivity'.

The union representative 'Oh please, don't blame employees. The productivity is high! I'm not here to discuss reductions in pay or redundancy plans'.

The employee's representative argued, 'How can you have such different opinions and figures about the very same firm?' ….

Finally, we found a solution and I'm still working at Step plc. What is interesting in the story is that it's a typical example of discussions you can encounter in a meeting where different stakeholders are involved. My long experience as CFO teaches me that people tend to think about accounting and finance as a subject with only right or wrong answers (I mean, look at the employee's conclusion). In reality, in accounting and finance there is no such thing as a right/wrong answer. In fact, I found that different stakeholders look at the same thing differently not only in management, strategy, operation, marketing, but as shown above, in accounting, too.

I think there are at least two main reasons behind such different perspective:

Firstly, each stakeholder is interested on specific topics and runs analysis accordingly: for instance, my main concern as CFO is to pay attention to accounting standards while the bankers focus attention on the firm's financial aspect and CEOs are interested in the big picture by looking at very general figures. Both tend to forget that the figures they rely on can be affected by the accounting standards I used. The union representative and the employee will be focused on the role of human resources in the organisation, their impact on the costs and on their productivity. To sum up: your role affects the way you look at the firm.

Secondly, technically speaking accounting and finance rely on assumptions that are often taken for granted and not explained or discussed. Different assumptions can affect the way in which you calculate ratios: ROS is the 'return on sales' but its calculation depends on what you consider return and how you calculate sales. So, it's important to always have in mind the assumptions behind the calculation and to be able to discuss them with other stakeholders.

So to sum up - there are different interests, different perspectives, different analytical approaches, and different conclusions. I know it can seem quite strange but finance and accounting is always a matter of perspective and assumptions.

My story stresses an additional point: the jargon. I and all accounting and finance people are often blamed for using very complex and incomprehensible words, acronyms and so on.

And it's partially true, but the terminology, as well as the acronyms used help us in exchange of information. At the end of the day, each sector tends to develop its specific jargon: finance and accounting is no different. My opinion is that it's important for people who work in other departments to get to get used to it as well as to be able to challenge CFOs on the meaning of the jargon used.