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3 Reasons Why Technical Leaders Should Understand Finance

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Why should technical leaders take the time to learn business finance? Although these leaders are most valued for their technical skills, it's important that they develop business acumen as they grow into roles with broader influence. Financial training will benefit a company in three areas:

- **Dexterity:** In the post-2009 economic environment, leaders with better cross functional understanding increase a firm's dexterity to respond quickly to changing pressures in the business environment.
- **Decisions:** Broader management skills translate into better decisions, better execution of projects, and better business performance.
- **Depth:** Deeper business skills improve emerging technical leaders' career satisfaction and provide a strong pool of management talent on which the company can draw for higher level positions.

Overview

Even though technical leaders are most valued for technical contributions, companies should invest in basic financial training to develop their business skills.

This investment increases organizational dexterity to deal with a more dynamic post-2009 economy; improves the quality of decisions for better outcomes; and builds depth in the company's talent pool.

Consider an example. Ann, the CFO, is rushing through the cafeteria to her next meeting and bumps into Bob, the engineering VP. The annual budget was finalized two months ago, but Bob has just discovered some valuable new design tools that aren't in his budget.

The conversation might go like this:

Bob: "We need to spend \$500,000 on new design tools! Everyone's *really* tired of what we've got, and it would make us a lot more productive."

Ann: "Sounds good, but it's not in the budget. Be sure we look at it next year."

One of a firm's critical challenges is building the dexterity to respond to a dynamic business environment.

Or, it might sound like this:

Bob: "I just discovered we could earn 18% on a \$500,000 investment in design tools by improving productivity and time to market."

Ann: "18% is a pretty good return! Email me your figures and let's ask the executive council for contingency funding next week."

Dexterity

In the first conversation above, the company will let the new tools opportunity languish until the next planning cycle. Bob senses the value of the new tools, but without a working knowledge of finance, he can't explain it to Ann in terms that will get her support for quick action.

A study by IBM conducted interviews with Chief Officers around the globe about the challenges they foresee in the post-2009 economy. One of the critical challenges they identified was improving their firms' dexterity to respond to an increasingly complex and dynamic business environment.

“Organizations unprepared to act immediately on new opportunities may watch them slip away from their grasp almost as quickly as they emerge.” (1)

Such organizational dexterity demands strong cross-functional collaboration without the burdensome overhead of formal approvals across organizational boundaries. In turn, this requires that leaders at all levels have the knowledge and skills to understand business issues and collaborate effectively to recognize and quickly respond to external changes.

Management experts often observe the need for technical leaders to collaborate with customers and with marketing, manufacturing, and quality functions. It’s curious that these experts rarely mention collaboration with the finance function. Without a working knowledge of finance, technical leaders are unprepared to quickly recognize and gauge the impact of significant financial issues. Waiting for the next formal management review can cost valuable response time.

Decisions

In the second conversation above, Bob has already estimated financial returns on the tools investment and made the decision to seek funding. If his analysis had shown poor returns, Bob would have discarded the idea without the need for higher level involvement.

It’s curious that management experts rarely mention the need for collaboration between technical and finance functions.

The economic value created by a business is the aggregate result of decisions made at all levels in the organization. Senior managers’ top level decisions set direction, but can create little value without the effective execution that results from sound tactical decisions at all levels of the organization.

The authors of a report published in McKinsey Quarterly write that product development process improvements have reached a plateau in recent years. They observe that yesterday’s rigid development processes were designed to limit the negative impact of weak project management, but these same processes limit the potential contributions of the best leaders. They suggest that firms need to develop good management talent and observe that “the most valuable employees have experience in several technical functions as well as some business training.” (2).

Senior managers’ high level decisions create little value without good tactical decisions to support them.

When the organization has a cadre of managers with business skills, decisions at all levels are better aligned to carry out top level direction. Technical leaders’ business skills must go beyond budgeting and expense management, which they learn by experience. A working knowledge of business finance includes understanding financial statements and financial performance, investment metrics, and how technical decisions impact financial value creation.

Many decisions commonly made by technical leaders impact financial performance, for example:

- Selecting a new product portfolio to drive strategic progress, while optimizing investment returns;
- Balancing risk and return in new product investments;
- Comparing financial benefits of short and long term projects;
- Evaluating capital investment in design and manufacturing tools; and
- Making mid-project tradeoffs involving development expense, schedule, features, and unit cost.

Technical leaders need knowledge of business finance to improve economic value. Simply codifying these important decisions into process recipes and infrequent management reviews does little to align activities with business goals in a complex and dynamic market.

Depth

In the first conversation above, Bob fails to convince Ann of the value of the new design tools. This not only delays an important business decision, but is usually be a source of frustration for Bob. He

may mutter to colleagues that “bean counters” just don’t understand technologists’ needs, amplifying misunderstanding between technical and business leaders.

Training and development expert Elizabeth Gold cites research showing that 85% of an individual’s success depends on the ability to deal successfully with other people (3). As they move into more responsible roles, technical leaders need the skills to participate in broader business discussions. Without financial training, emerging leaders often find themselves at the periphery of important business discussions.

When technical leaders have a basic understanding of finance, the company has a deeper pool of management talent with knowledge of how technical activities impact other business functions and the ability to discuss that work with financially oriented executives.

Equipping emerging technical leaders with business acumen—even when the leaders are on a purely technical career path—not only enhances the leaders’ scope of influence and job satisfaction, but also makes the organization function more smoothly without misunderstandings and unnecessary intervention from top managers.

Contact

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Notes:

- (1) IBM Corporation, Capitalizing on Complexity – Insights from the Global Chief Officer Study, 2010, April, 2010 p 54, available at <http://www-935.ibm.com/services/us/ceo/ceostudy2010/index.html>
- (2) Richard Holman, Hans-Werner Kaas, and David Keeling, The Future of Product Development, McKinsey Quarterly; 2003 Issue 3, p 38 available at <https://www.mckinseyquarterly.com/PDFDownload.aspx?ar=1334>
- (3) Elizabeth Gold, To the Point Training and Development, private conversations. <http://www.tothepointbiz.com/>