



The Role of Key Performance Indicators for Corporate Treasury

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This article discusses the background and consequences of treasury's developing role and the essentials of implementing relevant KPIs for corporate treasury.

Since its beginning in the 1980s, treasury has matured in a predictable way. From being independent from the rest of the organisation, it has now standardised the operations and processes, and with IT as the enabler it is becoming more integrated within the core operations. This requires the development of new sets of key performance indicators (KPIs) to measure and manage treasury from a group perspective. The choice of KPI and the manner in which it is implemented determines the success of the treasury.

Historically, treasury has been a black box to many parts of the organisation and thus treasury has been able to motivate its existence on its own terms. Basically, few outside of the treasury knew which KPIs to assign to them. This has meant that treasury, for a long period of time, has been excluded from close monitoring by the board and other stakeholders. The treasury was left alone and expected to manage risk, cash and funding. This has obviously lagged the objectives and development of treasury-specific KPIs connected to the overall company strategy. One particular example has been the treasury profit centre set-up that made up its KPIs as trading resulted, sometimes even partly generated, from margins on internal transactions.

However, in recent years, treasury has been increasingly integrated into the core business operations and placed into the company's overall context. This has usually led to treasury profit centres being transformed into cost centres. With time, the treasury has naturally matured as an organisation and consequently achieved a higher degree of integration with the corporate core business. Executive management has also become aware of the importance of the treasury's remit. This in turn has opened up the treasury for external scrutiny and expectations of more sophisticated KPIs better aligned with the corporate's strategy and overall objectives. This has led to KPIs becoming more developed and measured from both a qualitative and a quantitative perspective. Recently, we have experienced ambitious projects aiming to have all financial exposure and transaction management brought under centralised control and execution. The requirements of the treasury system's support is rapidly changing in order to fulfill the new demand and the treasury management systems should ideally be able to supply real-time financial information from the whole supply and demand chain, as well as providing functionality to analyse and perform scenario analysis and statutory reporting.

With the remit of treasury expanding substantially and with the emergence of the fully integrated financial supply chain, IT-based support systems will need to be adjusted and new solutions implemented. This will impose a greater complexity on the solutions and the implementation projects will demand much more sophisticated project management. Answerthink Inc. has conducted research on the success of system implementations focusing only on the technology aspects and neglecting the organisational changes required. The result was that only 22% of them succeeded to achieve the expected return on investment (ROI).¹ This means that KPIs endorsing proper change management in system implementations will be even more common in the future. The truth is that the only way to successfully implement and configure an application is to effectively connect processes, organisations and systems with one coherent set of KPIs related to business targets and human nature's resistance to change.

The new conditions imposed on the treasury has resulted in discussions within the treasury community asking 'what really is the treasury value-add?' (Read more here: [Achieving Treasury Excellence](#)) Sometimes this leads to philosophical and existential discussions about the future of treasury. Some treasurers miss the hay days of proprietary trading, while others look forward to the new opportunities of being part of new solutions such as supply chain financing and pension management. One thing is for sure: the conditions of the treasury change constantly and have to adjust to the global challenges of increased competition and cut-throat margins. It is necessary for the treasury to develop KPIs that are consistent with the company's overall strategy and objectives to excel its performance.

What is a KPI?

KPIs are financial and non-financial metrics used to quantify objectives. They are measured regularly to reflect and manage the strategic performance of an organisation. Important for a KPI is that it is easy to find and collect the information and, above-all, that it is easy to interpret what activities you must perform to improve the KPI. A common problem with using KPIs in measuring and managing is the complexity in finding and collecting the data because it is widely spread over the organisation. This is many times a minor problem for the treasury because of its limited size and closeness. However, with the increased treasury and company integration and the expansion of the treasury remit, it will be more challenging to develop and measure treasury KPIs in the future. There are several ways to categorise KPIs:

- Quantitative KPIs are usually set up to reach financial targets, such as cash reserves, head count, and financial risk limits.
- Qualitative KPIs are defined to measure non-quantitative targets that will improve behaviour of the organisation, e.g. how the treasury supports the group companies and the sales department.
- Directional KPIs are used to reach a more ambitious or different target than previously, often when changing the group's strategy or objectives.
- Actionable KPIs promote rapid and focused change usually during a limited period of time such as system implementation or a company merger.

The components of a KPI lie in the information necessary and the tool to compile it. Increasingly a KPI fails because it is too cumbersome to find and collect the underlying information. It can be spread over a number of different databases or it can be stored as different types of time series. For example, when collecting daily account balance information from all the group's bank accounts worldwide, the date can differ from when the cash actually is available. And if we require statistics of what kind of transactions the data consists of, it may be impossible and there might even be differences in methods and possibilities to collect historical information. So besides being relevant to measure, the information that builds up the KPI must be easily accessible.

Types of KPIs for Corporate Treasury

Different treasury-specific KPIs serve different purposes, and can generally be grouped into three different categories: process measures, treasury measures and treasury value-add (Table 1). Process measures are specific per process but generic in that they almost always cover cost, time and quality of the process. Treasury measures are specific in what they cover per area and process. As an example of a distinction between the two, cost can sometimes be split in both, e.g. hedge cost (bank fees, interest charges) belonging to the latter and processing cost (staff etc.) belonging to the former. Both are quantitative. Treasury value add is in a formative stage, closely linked to the remit of treasury, and arguably the hardest one to measure, or rather, the hardest measures to interpret since they are qualitative.

Table 1: Different Categories of Treasury-specific KPIs

Process Measures	Treasury Measures	Treasury Value-add
Cost Time Quality (error rate etc.)	Forecast accuracy (comparing forecasts with actual figures) Hedge cost Funding cost (comparing actual rates with benchmark e.g. 3M treasury bills)	Business unit partnering Client satisfaction (surveys, balanced scorecard) Balance sheet and income statement improvements (economic value add, connecting treasury to the supply chain)

Over the years different models have been developed to simplify the developments and measurements of KPIs. The best KPIs combine measurements of several perspectives and are easily understood. Not being too treasury-specific, as two of the most successful examples we can mention economic value add (EVA) by Stern & Stewart² and the balanced scorecard (BSC) by Norton and Kaplan.³

Among the strengths of EVA is the connection it imposes between the performance of the balance sheet and the income statement avoiding any one of them to cannibalise the other. This methodology can, for example, be used when implementing a supply and demand chain financing solution. Another strength of EVA is that it adjusts so that statutory accounting (GAAP and IFRS) is not developed for analysing a going concern. Instead the accounting rule base is developed to protect stakeholders at a potential default situation and can therefore create ambiguity of the relevance of a financial KPI.

The advantage of the BSC methodology is that it effectively assists in raising the organisation's perspective to those of the customers and other stakeholders. BSC also decreases the focus on historic information and instead creates an urgency to achieve future results.

Business unit partnering connects treasury to other parts of the organisation. Strategically aligned KPIs will help the organisation to gather, analyse and report the information necessary to remain on top of. For example, if an organisation wants to understand and manage its true commercial foreign exchange exposure included in sales, procurement, offers, etc, the information is hard to gather ad hoc. However, a KPI measuring the exposure coupled with right incentives will create a situation where the group staff automatically will gather all the detailed information, collect it, analyse and report it.

Client satisfaction is usually measured internally, i.e. the 'client' is another business unit. This can be done through four phases:

1. Understand the client expectations. Treasury must know the client specifics and what they expect from them.
2. Set goals. Exceeding the expectations means delivering more than what the customer has specified. In theory this implies that the service treasury delivers to the client must be better than the competitor's, i.e. the bank.
3. Execute. Once the improvement goals have been determined, treasury acts on them, measuring progress regularly.
4. Audit customer satisfaction. With some pre-determined regularity, treasury should ask the client to evaluate the service received, usually through surveys that should be interpreted with weighted scores according to the stakeholder.

Client satisfaction can also be measured externally, i.e. the 'client' is a supplier, distributor, or end user, as we may see increasingly when treasury is connecting more and more with the supply chain. The qualitative nature of external client satisfaction may spark a debate about who should have the ownership for such KPIs. However, quantitative external KPIs already exist, especially for working capital management (WCM), the most common KPIs being cash conversion cycle (CCC), days sales outstanding (DSO), days inventory outstanding (DIO), and days payable outstanding (DPO). If measuring both qualitative and quantitative external KPIs, the corporate will find out whether the benefits achieved through the quantitative KPIs, e.g. low or negative CCC, are sustainable and not harmful in the long term for its supply chain.

Both long-term and occasionally short-term KPIs should be considered. Long-term KPIs are usually quantitative and qualitative, and short-term KPIs directional and actionable.

The long-term KPIs eventually change the core values of your company. It is interesting to investigate a company's core values and how they have evolved over time. One example is how the risk willingness has changed in organisations that sometime in the past experienced massive losses on speculation in, for example, foreign exchange or the commodities market. When the losses become official, the board introduces risk adverse policies and KPIs that, with time, determine the treasury policy, the system choices, the treasury organisation and targets, etc, for a long time. The core value eventually changes from risk willingness to risk aversion through the choice of KPI.

Long-term KPIs usually have two different scopes: either they are meant to keep up targets that are part of the overall performance of the company, for instance interest rate net and cash reserves, or they are meant to achieve continuous improvements, for instance when you want to achieve less errors in the flow of the treasury's transactions, less working capital and higher level of cash centralisation.

Short-term KPIs, as the name suggests, support change management during a short time-frame. There is word for caution when using short-term KPIs - if you change KPIs with too short intervals there may be a risk that you just create confusion and desperation through the staff not fully understanding the reason behind and purpose of the KPI, and thus not understanding what behaviour is expected. A KPI is a powerful tool but must be properly defined, implemented, understood and accepted by the organisation. A KPI must be able to gain your organisation's respect otherwise it will be disregarded. This is avoided by having a tight link between change management objectives and short-term KPI objectives.

How to Benefit from KPIs?

The benefits of KPIs are twofold: a means for continuous improvement and being inline with group strategies and targets, and a prerequisite for being able to benchmark against other treasuries. What should be done to attain these benefits?

A KPI must be measured regularly and consistently. Very rarely this is possible without IT system support. The lack of system integration and the ambition of companies to force technical integration by performing organisational integration first often creates a Pyrrhus victory. This leads us to believe that from an optimal KPI perspective, organisational change is usually best performed by first changing the KPIs. When the new KPIs are accepted and the organisation is aligned to perform in accordance with them, the formal change of the organisation can take place. In the best cases we have seen, the organisation itself requests another chain of command and descriptions of new and updated roles and responsibilities to facilitate a good performance of the KPI.

A successful KPI should be able to contain the strategic, tactical and operational aspirations of the organisation. It should be easy to visualise and understand. It should never be ambiguous and should not be in conflict with other KPIs or rules and regulations. A successful KPI is also validated continuously, and over time it becomes one of the virtues of a company and assists in building up its values and guiding principles. A successful KPI is part of the company's DNA and assists the organisation in performing its long and short-term prioritisation and ensures that the employees are guided in their work and spend as much time as possible on value-added activities.

Moreover, a successful KPI is supported and incentivised by the management. It is not harder (or easier) than raising a family; your children do what you do, not what you say. Rewarding and punishing the organisation in accordance with the KPI should be the norm.

When to Introduce KPIs?

The old adage that 'what is not measured does not exist' applies to all organisations. The existence of relevant KPIs is an absolute must for any organisation if it is to survive. In today's competitive and fast-moving environment, a consistent KPI used over the long-term becomes the bearer of the company values and aspirations and is the skeleton you hang your organisation on.

We would argue that it would only make sense to introduce a long-term KPI, with its full metric and measurement, in an organisation that is reasonably mature with regards to having experienced most of the sides of its business and its expectations. Introducing a KPI in a treasury that is just about to be defined, or just about to be set-up, would not benefit from an introduction of a long-term KPI. Such an organisation should be more occupied with driving fundamental changes, working towards setting out short-term KPIs, tied to any over arching treasury strategic vision.

The short-term KPI should be introduced when you require fast and firm change. This is most common when you implement a new system or when you change the organisation dramatically through, for example, a merger. For the complete success of a system implementation, it is essential to use KPIs that support the overall objective of the project without limiting them to being merely IT related KPIs. The objectives of a treasury system implementation are always to improve the organisation's performance with the assistance of IT. This requires KPIs that easily combine the measurement of success over the three factors: processes, organisation and systems. Even if you implement KPIs early on, they create no effect if they are not diligently used throughout the whole duration of the project and kept for a sizeable time thereafter to enable comparisons between the new and the pre-project performance. Thus a discipline approach substantially increases the chances of your organisation to realise the true potential of your investment.

How to Introduce KPIs?

When trying to introduce KPIs for corporate treasuries, it is usually never enough to simply decide on KPIs and start measuring. It is important to first take a step back and understand and acknowledge the group contextual matters for treasury before introducing a KPI.

We would argue that treasury is the most polarised of all group functions; by not only having its own discipline, it is also active on the financial market being completely different in nature and convention than where ordinary group business is being conducted. This observation has the same characteristics as a double-edged sword, cutting two ways is as harmful as helpful.

It is potentially harmful if an implementation is performed in isolation and, for example, only tied to a KPI that promotes more the pure performance on the financial markets rather than leveraging group objectives. Such an approach also alienates treasury from the group rather than addressing the integration.

But is helpful if using correctly implemented relevant KPIs which (i) measure and assess value/performance directly to the group and (ii) measure and assess value/performance with other treasuries. From the second pointer, it is important to understand that treasury by nature has more synergies with other treasuries at other corporations than synergies within other functions of the own group. Observing these factors will make the KPI an excellent tool for continuous improvement over time and a communication tool for group management.

To evaluate, navigate and prioritise, one must understand the organisational maturity and capability of the group, as well having a good understanding of the maturity of the market where the group is active.

Empirically, we have seen that the approach to implement KPIs have two distinct phases; (i) a top-down phase which is recursively working its way through six defined areas and (ii) a bottom-up approach to facilitate the implementation of the KPIs.

The top-down phase focuses on the complete understanding and description of the treasury. It is essential that KPIs represent something that can be measured and defined, especially for KPIs intended to have a longer life span. It is essential to apply a proven method of how the treasury objectives and policies drive operations and how different components affect each other. From experience we have seen that a model with six defined and interlinked areas serves the purpose well (Read more here: [Achieving Treasury Excellence](#)).

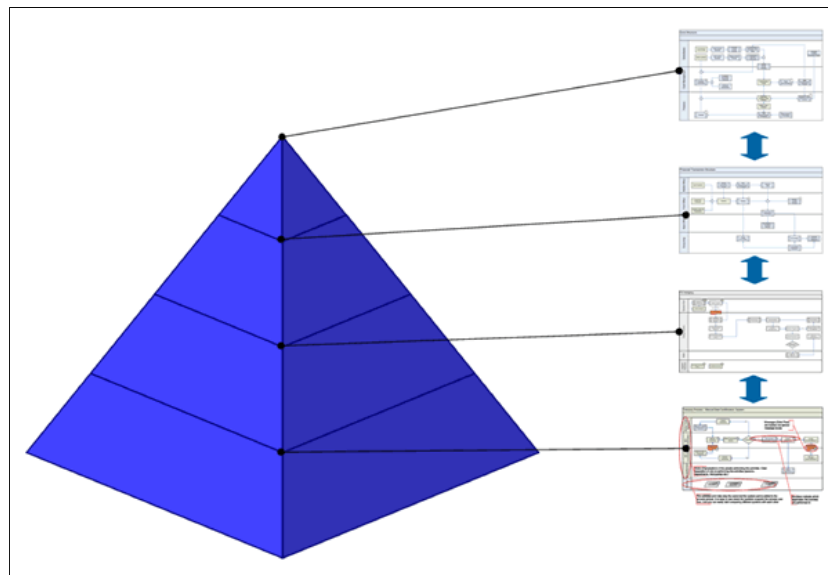
1. Treasury objectives - This includes the mission and objective that govern a treasury. Having completed the context assessment to the rest of the group, it will be a matter of revalidating it or otherwise defining it with senior management's expectations of treasury. The treasury objectives should be directly derived from the group's overall strategy and objectives.
2. Treasury governance and policies - From the treasury objectives a number of governance directives and policies are established, ultimately ensuring the treasury operations are performing according to corporate strategies.
3. Treasury processes - For each objective there are a number of processes to fulfill the objective. These processes shall be mapped and compared to treasury best practice.
4. Treasury organisation - In order to perform each activity within the processes and adhere to the policies, a treasury organisation must have pre-defined roles and responsibilities and chain of command.
5. Treasury data - The activities performed in the processes record, store, enrich and analyse treasury data and information. It is the enrichment and modification of this data that the activities are focused on, and, in turn, will ensure that the objectives will be met.
6. Treasury systems - The technologies used for storing, recording, enriching and analysing the data and information through the different activities performed by different roles.

Treasury's ability to contribute to the group's overall performance depends on the group's maturity level and crispness in its strategic roadmap and targets. By just the fact that the group has a treasury, there are some fundamental conditions fulfilled. From a KPI perspective, steps 1 and 2 are relatively static, but paramount to start the process of developing successful KPIs.

With the six-step approach you gain an understanding of how they are interlinked within the treasury. When addressing one step, it will have an impact on the other steps. Besides understanding the links, we also need to understand them separately to evaluate how changes to them affect others.

Figure 1: Hierarchical Introduction of KPIs for Corporate Treasury

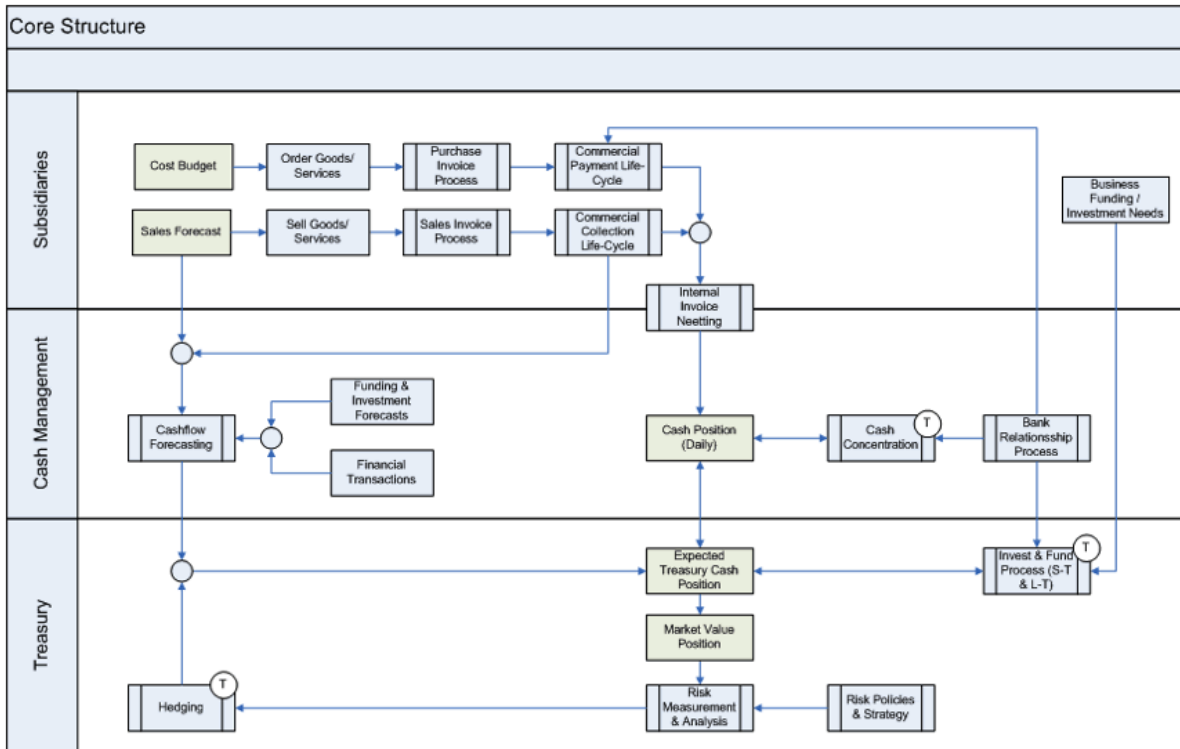
Figure 1: Hierarchical Introduction of KPIs for Corporate Treasury



During the exercise of mapping out the current operational environment, the development of KPIs considers what, how and which KPIs can be applied. Considering the hierarchical presentation in Figure 1, the tip of the pyramid will be where and how the treasury connects into the group. By using best practice template driven mapping, the development of corrective KPIs (directional and actionable) can take place - it will be quite obvious if the current situation is worse or better than the template.

We are clearly seeing the development of treasury being more of a key-group function than anything else, with the hands-on involvement in strategic matters as well as daily trade specific matters. Thus the areas of integration with the rest of the group is forming a best practice model, as represented in Figure 2.

Figure 2: Treasury's Core Structure and Group Integration



The best practice model is closely tied to the six step model and is built up in several layers. Comparisons with the mapping of the actual treasury processes and best practices identify areas to develop or destroy. The best practice model serves as the aspired to-be situation for your treasury. In that process, short-term KPIs represent the management tool. When reaching the aspired mix of processes, systems and organisation, the long-term KPIs are implemented to cement them in a continuous improvement cycle.

Conclusion

With corporate treasury stepping out of the anonymous 'black box', a means to measure its activities and performance is inevitably a requirement for most organisations. The benefits of KPIs are twofold: a means for continuous improvement and being inline with group strategies and targets, and a prerequisite for being able to benchmark against other treasuries. A good set of KPIs is a successful way to help your managers and staff prioritise their daily work. KPIs enable the micro-management from a helicopter perspective without having to have your nose in the details. If your organisation has the right KPIs it will allow you to focus on your tasks instead of meddling with those of your subordinates.

A top-down approach is suggested before introducing KPIs, taking into consideration the complete context of treasury, the group, and its stakeholders, and mapping out the relevant processes, goals and interfaces. Already by doing this, without KPIs, many improvement potentials become apparent. After that, a bottom-up approach will reveal what KPIs should be introduced for specific processes and how they should be implemented. Types of KPIs to be considered are process measures, treasury measures, and treasury value-add. Long-term KPIs will help treasury to be aligned with group objectives and strategy, and short-term KPIs are change management enablers.

¹'Best Practices Implementation (BPI)', http://www.answerthink.com/pdf/pdf_services/whitepapers/wp_bpi.pdf

²Stern J.M. and Shiely J.S. with Ross I. (2001), 'The EVA Challenge - Implementing Value Added Change in an Organization', John Wiley & Sons.

³Kaplan R S and Norton D P (1992) 'The balanced scorecard: measures that drive performance', *Harvard Business Review* Jan - Feb pp71-80; Kaplan R S and Norton D P (1993) 'Putting the Balanced Scorecard to Work', *Harvard Business Review* Sep - Oct pp2-16; Kaplan R S and Norton D P (1996) 'Using the balanced scorecard as a strategic management system', *Harvard Business Review* Jan - Feb pp75-85; Kaplan R S and Norton D P (1996) 'Balanced Scorecard: Translating Strategy into Action' Harvard Business School Press.