RESEARCH REPORT

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Overcoming obstacles to transformation in the finance function

Genpact commissioned a study through Pilgrim Partners LLC from September through December 2011. EVPs, SVPs, VPs and senior directors of targeted life sciences and pharmaceutical companies were surveyed to determine the key challenges and priorities facing finance and accounting (F&A), finance administration and commercial operations. Ninety of the hundred responses received were from executives at discrete life sciences and pharmaceutical companies in the U.S. and the rest in the U.K. Companies surveyed averaged 26,500 employees.

Overview

Given pending changes to a long history of blockbuster drugs and abundant pipelines, Life Sciences and Pharmaceutical companies now face market share loss due to a number of factors:

- Competition from generics
- Regulatory pressure
- Insurance company price controls
- Shrinking R&D pipelines

In addition, they must also meet a growing demand for innovative medicines to satisfy the needs of an aging population, keep pace with technological advances, and accommodate a shifting geographic mix to lower-priced markets.

Structural trends on top of increasing consumerization and tighter funding constraints will have an enormous industry-wide impact as well. Topping the list are far-reaching changes in the approach to chronic diseases, medical technology, social networks, global health issues, emerging markets and aging populations. Such pressures are compelling forward-thinking executives to respond with innovation in previously unexplored organizational areas, including transforming critical processes and systems to attain better information and more agile and responsive operations that retain customer loyalty.

Challenges create opportunities for change

Many executives surveyed report a shift in priorities to new and more innovative business models, but market uncertainty has many taking a more conservative approach to transformation, particularly those with new executives who are not ready to take risks. Even seasoned executives have shifted to risk minimization in response to rapid changes in pricing structures.

Although large firms have the resources and information to modify sales, risk and procurement strategies, they struggle due to cultural differences and incomplete post-M&A initiatives. Smaller firms, even those with strong and innovative leadership, find their options curtailed by weak brand penetration and limited operating structures.

Cost reduction plays a part as well, with sixty-eight percent of respondents citing the need to reduce costs as having the greatest potential impact on business. While innovation remains the key to success, unless organizations can gain traction on rising costs, transformation takes a back seat and promising new business models go unexplored. Still, an overwhelming majority of respondents (88%) agreed that their operational capabilities must improve, and the most progressive firms are moving ahead, with some taking an aggressive approach: standardizing systems to streamline reporting; improving FP&A capabilities through centralized processes; supporting collaborative partnering models; and adding shared service centers and outsourcing initiatives. All these measures add up to lower costs and more effective use of resources.

Achieving transformation

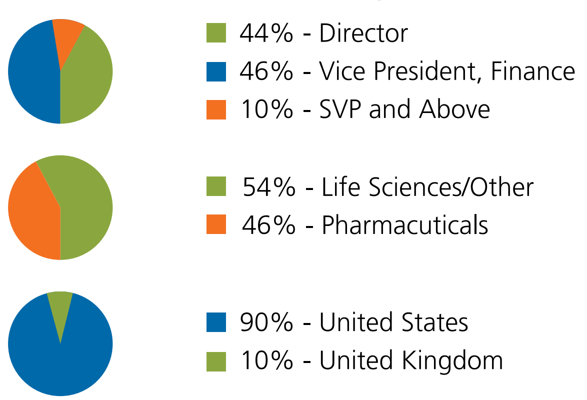
Achieving transformation means addressing the top challenges faced by respondents. While 68% said that the need to reduce costs topped the list of factors having the most impact in 2012, many found pricing and reimbursement pressures (53%), new regulations (33%) and increased competition (24%) to be strong factors as well.

Cost reduction

Half of survey respondents noted that transformation is expensive, and that it is difficult to make necessary changes within targeted budgets, but at the same time, many executives cited improving business processes (39%) as a means of reducing costs. These findings highlight how progressive companies are leading the way with transformational strategies that improve efficiency and performance while reducing the associated costs. Although both short-term performance and longer-term positioning are important, the former has taken center stage.

While 32% of respondents felt that all investment decisions must be driven by margins and that return on capital was a powerful driving force, concern over the trend toward generics (40%) is forcing attention toward cost-efficiency and effectiveness across the value chain. This is leading finance executives to assess how to improve systems and end-to-end processes enterprise-wide to lower costs and improve response to customers and market demands.

Research demographics



There is also a growing emphasis on infrastructure consolidation and R&D investments. Targeting technologies and leveraging new models, such as cloud technologies, can speed implementation and dramatically lower costs while improving overall efficiency and effectiveness.

Lack of information

This need for better data proved to be profound. Our survey revealed the number one barrier to improving organizational performance is a lack of real-time information for operations. Respondents want better performance management tools and "Big Data" analytics for predictive decision-making. Access to external data, including distribution and patient data to support local forecasts, is essential to developing the transformational new business strategies that lead to increased growth in new and existing markets.

Executives surveyed want improved analytical methodologies to attain new methods of distribution and better local marketing, including increased customer segmentation/ targeting and internet distribution. Others hope for improved understanding of pricing and demand management while refining distribution strategies in emerging markets.

Executives felt that technology to coordinate decision-making is a dominant initiative for improving operations, emphasizing the need to upgrade both standard reporting systems and business intelligence/predictive analytics applications. Organizations that are targeting analytics as a primary component of operational improvements ensure access to the information needed to make powerful decisions and formulate targeted marketing and sales plans that will increase their market share and drive up revenues. Innovation in acquiring the necessary real-time information to support operations could prove a critical differentiator for life sciences companies in the race to seize opportunity and forge ahead of the competition. Respondents overwhelmingly agreed that their firms were not prepared to handle the transformational changes taking place within their business models and expressed concern that the overall culture remained opposed to change. They identified barriers such as:

- Lack of real-time information for operations and execution (55%)
- Lack of process standards and discipline (44%)
- Lack of integrated risk management (44%)
- Lack of up-to-date information for strategic decision-making (42%)

Additionally, they felt ill-prepared to communicate across cross-functional groups.

Consumerization and price

The new world of expanding choices is driving stronger competition and vastly elevating the role of brand strategy and customer loyalty. Sixty-one percent of respondents chose "improving brand and customer loyalty" as their number one strategic priority, followed by "optimizing commercial operational processes" (56%) and "developing a strong R&D pipeline" (49%) over the next three to five years. Forty-eight percent agreed that future growth would be in emerging markets, though they also stated that local research and manufacturing were critical to meeting local needs.

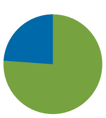
Companies who move to connect better to customers with more integrated global systems, more responsive workflows, and clearer insights into customer behavior and market trends will emerge as winners from the current economic uncertainty.

Trends in finance

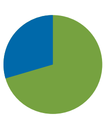
Finance managers seemed most aware of the relationship between improved internal business processes and improved efficiency and performance. Seventy-eight percent cited this as the top consideration for reducing costs, followed by information technology investment (72%) and decreasing supplier costs (68%).

Most finance organizations believe that their capabilities in transactions and controls are slightly above "capable" but well below "highly capable." With regard to strategic financial performance, 50% said that performance is stagnant or declining and feel that local planning and analysis expertise is not coordinated with corporate decision-makers. Significantly, about one-third have not progressed at all with business performance monitoring and integration of information across the enterprise. Many companies find these business and organizational complexities too difficult to tackle through major initiatives. They are taking small, conservative steps through targeted reorganization and systems improvements to drive efficiencies and cut costs. The most successful are using these initiatives to achieve best-in-class process performance that in turn lowers overall cost while simultaneously improving the company's ability to attract and retain customers.

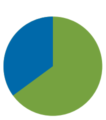
Key survey findings



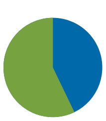
- 76% are improving financial systems to address reporting and forcasting capabilities



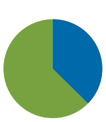
- 72% are developing talent to address new enterprise requirements



- 66% are improving the cost effectiveness of core finance activities



- 48% are expanding the presence of the finance function geographically



- 42% are investigating outsourcing options

Partnership is gaining ground

Some 42% of respondents, particularly those from larger firms, are willing to assess F&A outsourcing. Many finance executives see their organizations transitioning toward a strategic partner role, viewing expansion of FP&A capabilities and improvements in systems as a means to provide both financial stewardship and strategic financial guidance. Younger, emerging firms, less mature in international expansion, seem more interested in core finance support and are less closely engaged in strategic issues. In either case, an experienced partner can facilitate small or large-scale projects through ready availability of resources and immediate application of best practices to drive the necessary improvements.

Better decision-making is critical

For organizations focused on strategic finance, improving decision-making across the enterprise is the top priority. Finance facilitates enterprise-wide information and decision-making, but integrating this information across the enterprise, managing risk, and reducing costs are critical areas for improvement. Key initiatives include:

- Improving financial systems to address reporting and forecasting capabilities (76%)
- Developing talent to address new enterprise requirements (72%)
- Improving the cost-effectiveness of core finance activities (66%)
- Expanding the presence of the finance function geographically (48%)
- Investigating outsourcing options (42%)

Innovation is a key differentiator in achieving more accurate and more timely information. Companies are looking at cloud solutions and technology tools that facilitate global access to integrated information sources, as well as better reporting and detailed, industry-specific analytical tools that aid the decision process and provide clear insights into day-to-day operations.

Risk, scale, complexity and resources may deter transformation

Nearly sixty percent of finance executives consider transformation to be risky, and with good cause. Leaders must provide processing, controls, reporting and strategic services even when strapped for resources. They must also proactively address coordination issues across different markets and geographies. The resulting strain on existing business operations can take a toll on performance.

Wide-scale changes are costly as well. Half of the executives surveyed cited budget constraints as the number one deterrent to making the type of organizational changes that could deliver the most benefit. Still, progressive companies continue to implement new operating models by making changes on a smaller scale, hoping to realize stronger benefits over time.

Recommendations for achieving effective transformation

Companies that limit their approach for improving revenue performance to emerging markets, mergers and acquisitions, and cost-cutting will eventually fall prey to the law of diminishing returns. The true leaders in the life sciences and pharmaceutical industry are embracing a more comprehensive means of improving cash flow, margins, revenue and brand loyalty. These companies are focused on achieving best-in-class process performance, engaging with strategic finance partners, implementing more robust decisioning strategies and tools and offering greater coordination across markets and geographies, which will in turn drive greater effectiveness across global operations.

Opportunities for transformation abound for companies that apply performance metrics in a number of operational areas, including:

- R&D and commercialization, collaboration
- Active management of outcomes
- Emerging market product offerings
- Micro-segmentation of products
- New operating models
- Multiple business models
- Consumer branding
- Information management
- Compliance and safety regulations
- Shift in funding mix

This survey demonstrates that life sciences and pharmaceutical executives are aware both of the need for change, and of the primary challenges to transformation. It also shows that the underlying issues can best be addressed by a combination of better information, stronger processes, and integrated technologies that facilitate responsiveness to both opportunities and challenges.

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