3 CFO Priorities for 2022

CFO | ORACLE NETSUITE

The economy may be recovering, with 2021 Q4 GDP clocking in at an annual rate of 6.9%, but inflation is at record levels, interest rates are rising, the labor shortage persists, and conflict in Europe promises to add to ongoing supply chain challenges. CFOs, with their unique insights into the financial forces that affect all organizational areas, are needed to help lead their organizations through a mixture of knowns and unknowns.

In preparing their organizations for a stronger, more resilient future, CFOs must focus on creative and careful approaches to cash management, proactive approaches to wage and workforce management, and purposeful scenario planning.

Get Creative with Cash Management

Throughout 2021, companies largely raised cash to strengthen their balance sheets and invested according to board-approved provisions of their investment policies, says Jerry Klein, managing director at Treasury Partners, a New York City-based investment firm that provides corporate cash management services to private and publicly traded companies.

These policies were designed to pursue the three priorities of safety, liquidity, and yield.

But the first quarter of 2022 brought changes and new challenges, driving CFOs to take a renewed look at their cash holdings and plans for liquidity.

> “A combination of factors led to a dramatic rise in short-term interest rates during the first quarter of 2022. This has enabled companies to extend maturities on their corporate cash to achieve higher returns.
>
> **Jerry Klein, Managing director, Treasury Partners**

CHANGES FOR 2022

Record levels of inflation over the past 12 months have driven the Fed to start increasing short-term interest rates. As a result, companies must evaluate their options for managing cash amid a rising rate environment, which can include working with their bank, finding alternative financing, and updating existing lending terms to stay liquid.

“A combination of factors led to a dramatic rise in short-term interest rates during the first quarter of 2022,” Klein says. “This has enabled companies to extend maturities on their corporate cash to achieve higher returns. In addition, given the significant spread between money market yields and short-term treasuries, companies have begun laddering short-term treasuries for further yield enhancement.”

The Fed is expected to continue raising rates throughout the course of the year, but a large portion of the expected Fed tightening is already reflected on the front end of the yield curve, Klein says. He recommends that corporate investors start extending maturities and pushing out the weighted average maturity of their corporate cash portfolios to take advantage of the rising yield environment.

TOOLS FOR CASH MANAGEMENT

More change is likely on the horizon, with ongoing global conflict, resulting supply chain challenges, increasing wage pressures and ongoing inflation. To keep their organizations solvent, CFOs must be prepared. "All corporate cash should be invested under a board-approved investment policy," Klein says.

For smaller companies, especially those experiencing substantial growth to date, they must take this opportunity to protect their cash positions. "Small but growing companies must adopt a board-approved investment policy," Klein says, and "companies that are burning cash should update their cash forecasts monthly," with the company cash manager keeping a firm pulse on free cash flow.

> "All corporate cash should be invested under a board-approved investment policy."
>
> **Jerry Klein, managing director, Treasury Partners**

To free up additional cash, a recent McKinsey report recommends financial executives carefully review the assets and liabilities on their balance sheets that may normally be overlooked. For example, they might look for ways to recover cash that may be trapped among joint venture partners or foreign subsidiaries; or single out low-performing assets for sale or repurposing.

For growing companies that rely on spreadsheets and static data to forecast future cash flows, this can be a particular challenge. Hours spent gathering the data needed to develop forecasts become costly, and this labor-intensive process is repeated every time the company needs an updated forecast.

Investing in a cash management solution, ideally before cash reserves become too tight, can automate this process and provide real-time insights into current cash position and near-term cash flow. Dashboards offer links to cash management activities and display cash balance, accounts payable and accounts receivable balances, and cash flow trends. Having this information at their fingertips allows finance teams to make faster, better-information decisions.

For those companies incorporating debt and equity securities into their capital structure and investing cash flows, CFOs should "confer with accounting professionals to determine the proper FASB 115 elections" and its classification and impact on cash flows.

"Most corporate cash investors utilize the 'Available for Sale' designation, which enables the sale of securities prior to maturity, while reflecting unrealized market value changes in other comprehensive income within the equity section of the balance sheet," according to Klein.

Approach Wage and Workforce Management Proactively

Despite the economic recovery underway, economists see unusual trends in wages and the workforce. The first is the severity of the labor shortage, which has a direct impact on companies' growth potential, says Gad Levanon, chief economist at The Burning Glass Institute. Currently, the unemployment rate is 3.8%, but the labor force participation rate remains below pre-pandemic levels. As job growth continues and in-person service industries, previously stifled by the pandemic, strain to grow, unavailability of qualified skill will begin to impact revenue and operations.

"By the end of the year, we'll be perhaps below 3% unemployment rate, which would be the lowest in 70 years," Levanon says. "For the foreseeable future, we are likely to be at a very low unemployment rate environment and difficulties with recruiting and retention will remain." Unemployment, often uncritically viewed as "the lower the better," in this case means the opposite; because the base of available (and qualified) workers has diminished so greatly, it is below the natural unemployment rate and can impede long-term economic growth.

A second trend that demands CFOs' attention is the shift to remote work, which greatly affects not only how people work but where they work, driving vacancies in city centers and huge home improvement increases. The trend also offers opportunities for companies to hire people in far-flung geographic locations.

> CFOs... always have to pay attention to what's happening in the labor market and the workforce. But now, because of the severity of the labor shortage and the movement toward remote work, they... should pay more attention and be more proactive than ever before."
>
> **Gad Levanon, chief economist, The Burning Glass Institute**

"CFOs probably always have to pay attention to what's happening in the labor market and the workforce," Levanon says. "But now, because of the severity of the labor shortage and the movement toward remote work, they probably should pay more attention and be more proactive than ever before."

TOOLS AND TACTICS

CFOs face a daunting challenge, caught between their company attempting to grow while not having the human resources available to invest in. But there are tools and options available.

Create the right work environment. At Main Street Capital, companies have sought to attract and retain talent by raising wages, creating incentive programs and stressing culture and employee development, according to CFO Jesse Morris.

"Companies are spending a lot of time and effort on having the right work environment," says Morris. You've got to be competitive on pay, but at the end of the day you will also lose people if you don't have the right work environment—you have to give the opportunity for people to be challenged and grow."

Echoing Morris, companies are helping current employees gain the skills needed to "grow into" job vacancies via upskilling. Upskilling equips employees to evolve and grow in sync with advancement in technology and shifting business priorities. According to Accenture, both upskilling and reskilling -- instead of hiring new talent -- represents a 6x cost savings.

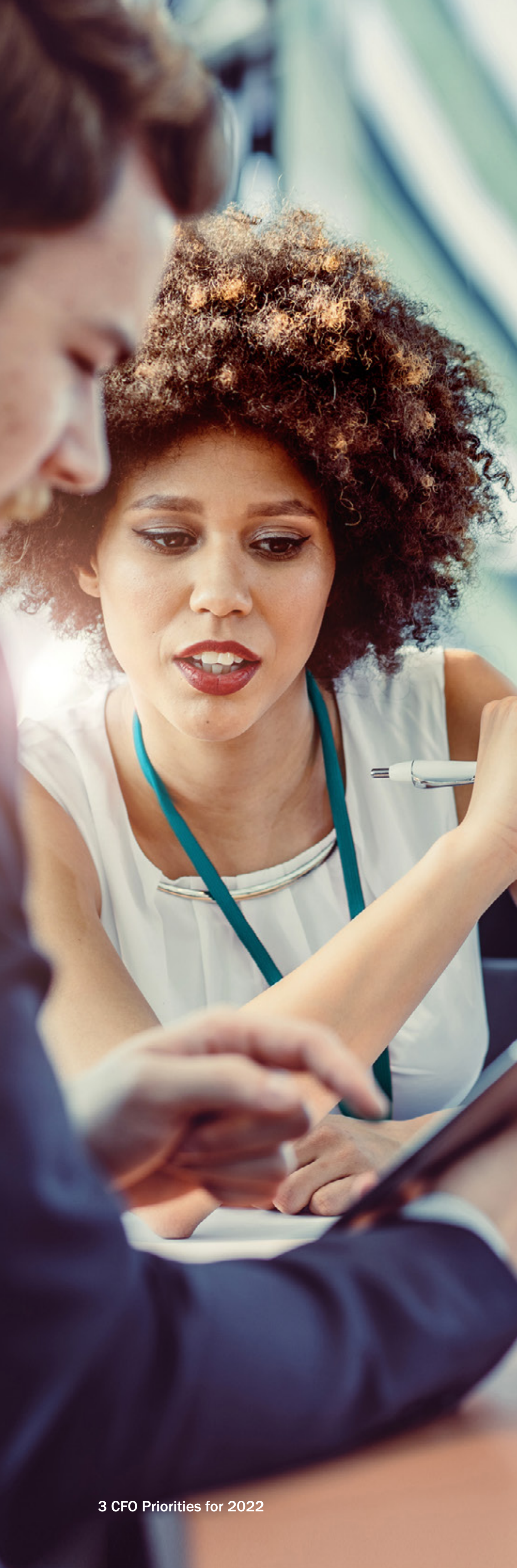
Expand automation. For several decades, manufacturing occupations were the most likely to be automated. But in recent years, routine office jobs have become the most likely candidates for automation, Levanon says. While automation may be a relevant solution across the company, it can be particularly helpful for financial offices to better manage a labor shortage.

Broaden your search. When seeking to hire new employees, CFOs can take advantage of the trend towards remote work by looking for candidates in geographical areas that have more available labor, and at lower cost, both inside and outside the United States, Levanon says.

Also, consider relaxing the minimum level of education or experience required for a particular job, and pursue demographic groups that are not typically part of your regular workforce. By analogy, "Before the pandemic, in response to the blue-collar labor shortages, we saw a big increase in the share of Hispanic women who are in the labor force," Levanon says. The same can be true for finance operations if CFOs work with HR to broaden the scope of talent acquisition.

Darden Restaurants, for example, is hiring some restaurant workers that it might not have considered qualified before. "Giving someone their first job and teaching them to do the things the way we do it is a good thing for us," said Ricardo Cardenas, Darden's president and COO, on the company's March 24 earnings call. "Maybe in the past, we would have said you needed to have a lot of experience in a restaurant before you [came] to work for ours."

Tighten the recruiting process. To secure more new hires, Levanon recommends shortening the hiring process by conducting fewer interviews and making faster decisions. CFOs can work with HR to tighten job descriptions, but there is a balance between narrowing the focus and accelerating the overall hiring sequence.



COSTS TO CONSIDER

As CFOs and their organizations manage current wage and workforce challenges, they must keep in mind several variable costs. Already, "there is unusually fast wage growth and unusually fast inflation, and they are feeding each other," Levanon says. "CFOs are very involved in wage determinations, and there's been a big jump in 2022 compared to 2021. Inflation is part of that, because there is pressure to keep up with the cost of living."

> The smart thing for CFOs to do is push HR people a little harder and say, 'What kinds of things will keep people here, and which ones are expensive and which are cheap and easy?'"
>
> **Peter Cappelli, Director, Center for Human Resources, University of Pennsylvania's Wharton School**

When it comes to costs, "the smart thing for CFOs to do is push HR people a little harder and say, 'What kinds of things will keep people here, and which ones are expensive and which are cheap and easy?'" according to Peter Cappelli, director of the Center for Human Resources at the University of Pennsylvania's Wharton School.

Cappelli points to signing bonuses and mental health referrals as two tactics inexpensive and appreciated by employees, compared to other benefits. Another action that CFOs can take is to determine the payoff from retention spending by gathering data needed to gauge the cost of employee turnover. "This is a pretty simply idea, but most employers have no idea of the answer, which is embarrassing—kind of astonishing" Capelli says.

CFOs must keep a close watch on potential costs and how they might factor into workforce and wage-related decisions.

Undertake Continuous Scenario Planning

After surviving two tumultuous years, savvy organizations are determined to avoid being caught off-guard by another disaster. And scenario planning is, for many CFOs, the best way to prepare for the unexpected.

"Scenario planning in 2022 is now a more continuous activity, where organizations are proactively monitoring the internal and external environment," says Philip Peck, vice president at Peloton Consulting Group. Scenario planning provides the framework for organizations to develop contingency plans and actionable playbooks that allow these organizations to deal with the volatility and complexity of today's environment.

> Scenario planning in 2022 is now a more continuous activity, where organizations are proactively monitoring the internal and external environment."
>
> **Philip Peck, Vice president,**
> **Peloton Consulting Group**

VALUE OF SCENARIO PLANNING

Robust scenario planning capabilities can provide organizations with a competitive advantage in several ways, Peck says. For example, scenario planning allows leaders to make decisions more quickly, better manage expectations and external communications, understand the financial implications of various scenarios, and seize new market opportunities.

For example, a leading toy manufacturer that relied on Asian suppliers identified supply chain constraints as part of their scenario analysis. They evaluated alternatives to expedite global shipments and committed resources to enable air shipments rather than traditional ocean freight. As a result, when the global supply chain came nearly to a halt, this toy supplier was able to satisfy the balance of expected customer demand for the Christmas holiday season, Peck says.

THE RIGHT DATA

For scenario planning to be effective, it's essential for organizations to have the right data. CFOs should first identify the data sets needed to support their modeling and planning efforts, Peck says. Often, the core financial and operational data needed is already available and being used for other planning, forecasting and analytic purposes.

"CFOs should work with their IT and business counterparts to establish a robust enterprise information architecture supporting a single source of truth for data and information," Peck says. "Modern data management and data integration platforms and advanced ETL / ELT tools (extract, transform, load), deliver access to high-quality data while minimizing manual efforts associated with data gathering, data manipulation, and data reconciliation."

Entrepreneurs and growing companies may be wondering how they can take advantage of scenario planning if they're not quite ready to invest in advanced tools. Here are three steps to get started:

1. Identify driving forces.

Start by establishing a timeframe and pull the historical data accordingly to evaluate variable factors. This will help you understand what was going on at the organization's healthiest point and the competitive advantage that you held during that time.

2. Brainstorm future scenarios, and templatize your plan.

Include external factors and consumer behavior as you build out your scenarios. Focus on two to three significant uncertainties and build out multiple scenarios from there.

3. Understand your planned response inside and out.

Each scenario should contain enough detail to assess the likelihood of potential responses' success or failure for the business. Once finance aligns and agrees with the responses, a framework can be created that helps the executive team make informed decisions. The results of any decisions made will need to be monitored in real-time so the team can adjust its ongoing response to a given event.

THE RIGHT SCENARIOS

To identify the types of scenarios for which to plan, Peck recommends considering a wide range of elements. They include, but are not limited to, geopolitical risk, the likelihood of economic growth or recession, raw material pricing trends, anticipated mergers and acquisitions, interest rates, talent and resource constraints, and supply chain disruption.

This is where finance teams can feel overwhelmed; there's no way to plan for so many possibilities properly. As stated above, the recommendation is to keep it as basic as possible by focusing on two to three significant uncertainties and building multiple scenarios from there.

In some instances, it can be worth undertaking scenario planning for current trends that seem to be spiraling. For example, labor represents the largest budget item for many organizations. As labor-related costs continue to increase, organizations must assess the financial impact and evaluate options for mitigating the financial impact of these higher costs, Peck says. Mitigation options might include price increases, greater automation, improved process efficiencies, and potentially strategic business model changes.

"Given the paramount importance of robust scenario planning capabilities in 2022 and beyond, CFOs should start now if they haven't already and work to improve their scenario planning expertise as fast as they can, with the awareness and understanding that some course corrections will be necessary along the journey," Peck says.

Scenario Planning Process Starters

Scenario planning can start by asking a core set of fundamental questions crafted in the form of a story or narrative, according to Philip Peck, vice president at Peloton Consulting Group. He recommends the following questions to get the process started.

- What is the demand for our products and services (units, price, & revenue) given the economic climate?
- How much inventory can / should we be holding, given supply chain disruptions?
- What happens if the economy goes into recession, and what happens in an expansion?
- If sales decline because of the conditions in Europe, do you know what actions you will take?
- How much capital will you need over the next 10 years, and how will you obtain it?
- What's going to be the use of that capital? What happens if you can't obtain bank financing?
- What would that mean for your business in both the short and longer term?
- What actions should you take around headcount management or support service levels in the event of a downturn?

Conclusion

CFOs are in a unique position to assume more strategic responsibility and take a more significant leadership role, mobilizing their financial acumen and insight to confidently guide their organizations through uncertainty and into a brighter future. To do so, they'll need to reconsider their approaches to cash management, wage and workforce management, and scenario planning. By focusing on these three priorities in 2022, CFOs can help prepare their organizations for a changing future.

SPONSORED BY NETSUITE

For more background on scenario planning NetSuite offers helpful templates and checklists.

Learn about how NetSuite automates cash management and how access to real-time data can help organizations make informed decisions about how and when to allocate cash.

ORACLE
NETSUITE

For more than 20 years, Oracle NetSuite has helped organizations grow, scale, and adapt to change. As the #1 Cloud ERP, NetSuite provides an integrated system that includes financials/ERP, inventory management, HR, professional services automation, and omnichannel commerce, used by more than 29,000 customers in 215 countries and dependent territories.

Learn more at https://www.netsuite.com. Like us on Facebook, and follow us on LinkedIn, Instagram, and Twitter.

Learn More