CFOs seize initiative in optimistic turn

Finance leaders pursue growth while reining in costs

Finance leaders are taking a contrary approach amid economic conditions that have been largely portrayed as gloomy, according to Grant Thornton LLP's CFO survey for the fourth quarter of 2022.

While the media has been quoting economists who are predicting a recession, the mood of CFOs participating in the survey was largely positive. The survey shows that CFOs ended last year with plans to go on offense rather than playing defense, despite the persistent inflation and seven interest rate hikes that punctuated a year of economic pain.

Respondents who were optimistic about the U.S. economy for the next six months outnumbered pessimists by more than two to one. The 54% of CFOs who reported being optimistic marked the highest percentage in the quarterly survey since 57% were optimistic in the fourth quarter of 2021 — months before runaway inflation led to rising interest rates and economic turmoil.

"In the previous quarter, we used the words 'cautiously optimistic'," said Sean Denham, Grant Thornton's National Audit Growth Leader. "Over the past quarter, the stock market has held its own, inflation has decreased and unemployment rates continue to decline, so there have been reasons for optimism. Everyone has been waiting to see what the Fed does on interest rates, but the focus is on the annual and quarterly earnings reports."

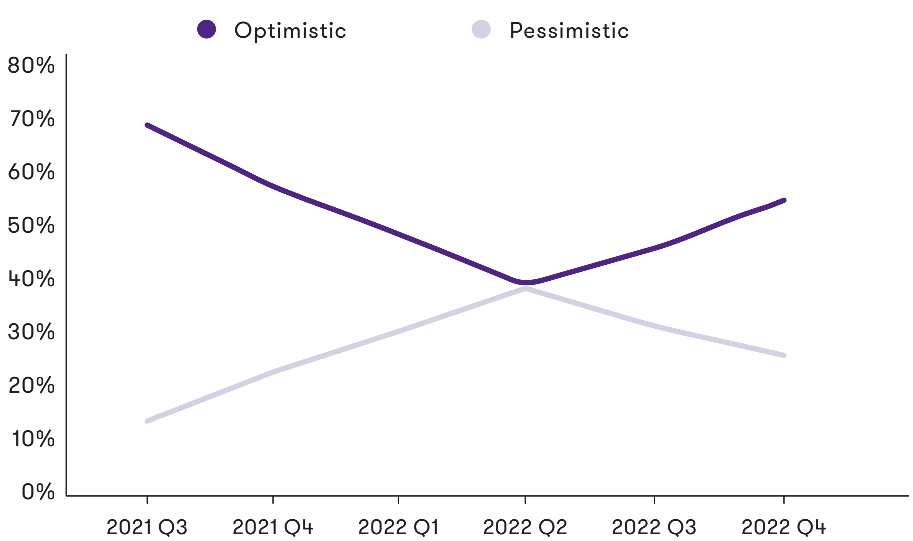
Chris Schenkenberg, Grant Thornton's National Managing Partner for Regional Tax Business Lines, said wage pressures seem to be softening for some businesses. Meanwhile, energy prices in the U.S. haven't yet experienced a price spike that many feared would accompany the winter weather while Russia's war in Ukraine is affecting the energy markets.

"It leads you down a path of, if there is going to be a recession, it might be a softer landing, meaning that interest rates are now high enough to where the Fed can lower interest rates and it will be relatively short-lived," Schenkenberg said.

CFOs' optimism extends to their own organizations as well. Sixty-one percent of survey respondents predict that they will experience net profit growth over the next 12 months, year over year, and 40% expect growth of 6% or higher.

Economic optimism climbs

Q: How would you classify your outlook regarding the US economy over the next 6 months?



Investing to get an edge

Even after precipitous interest rate increases, survey respondents show few signs of cutting investment in future growth or technological efficiencies that could give them an edge.

Four out of five CFOs said they plan to increase investment in digital transformation, confident that technological advancements present opportunities to operate more effectively with greater efficiency. In addition, 76% of finance leaders say they plan to increase investment in their financial planning and analysis functions and systems over the next year.

Chris Unruh, National Managing Principal, Technology Transformation for Grant Thornton, said companies only in a few cases are pausing between phases of an enterprise resource planning project, but most organizations are determined to complete this important work. “They may not start that next phase right away,” he said. “They may delay it a little bit, but in most cases, they’re continuing to move forward in some capacity.”

Meanwhile, a substantial majority of finance leaders plan to increase investment in their demand-generating capabilities (82%) and customer-retention capabilities (81%) over the next 12 months related to marketing and sales. Overwhelmingly, they are confident in their organizations’ capabilities in these areas, but there was an increase in 10 percentage points over the previous quarter in respondents who rated customer retention as one of their three biggest challenges. Thirty percent of CFOs now rate customer retention as a top challenge.

David Koppy, Principal, Strategy for Grant Thornton, said this focus on customer acquisition and retention reflects the overwhelming demand for growth at companies throughout the marketplace.

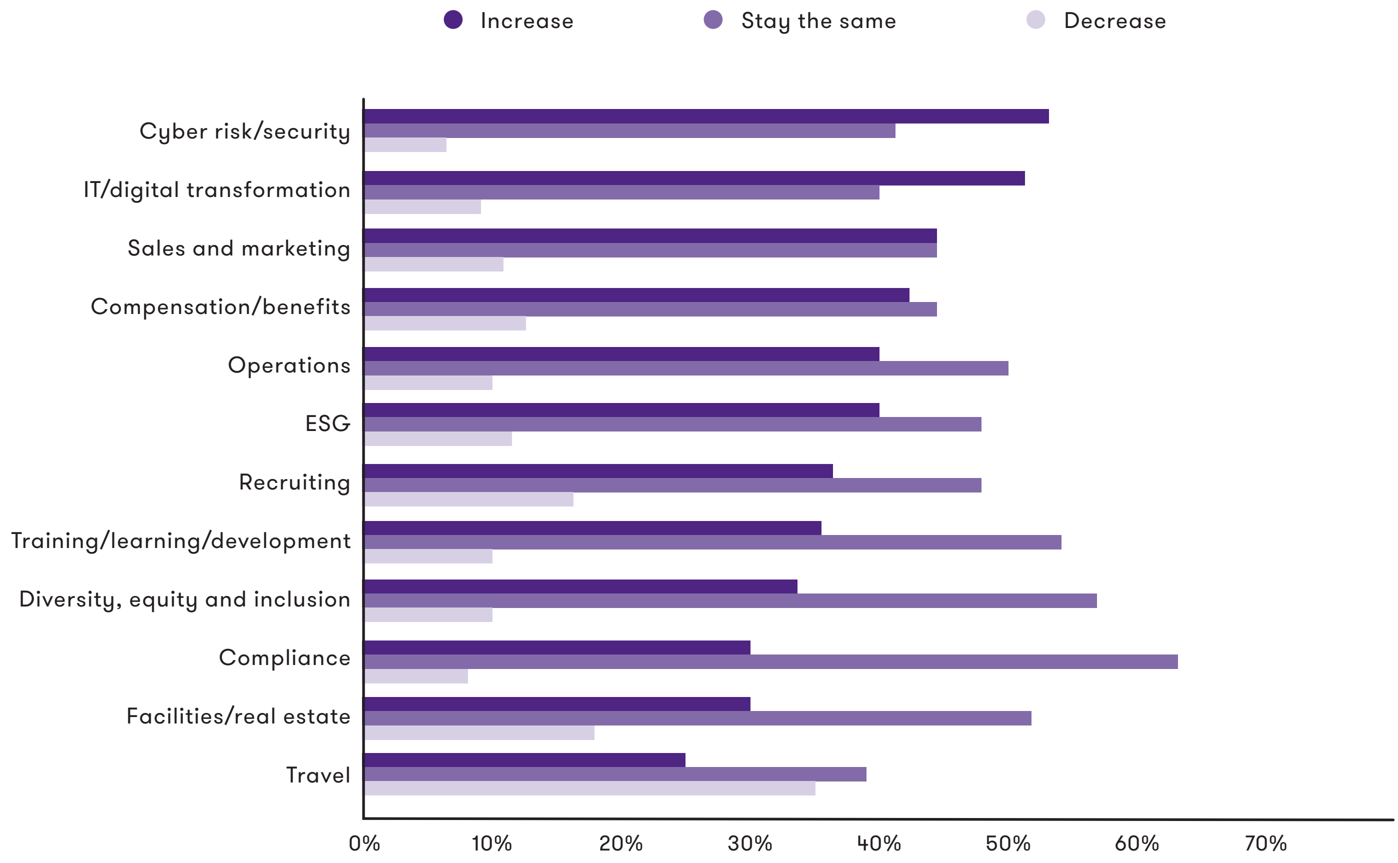
“Organizations are expecting sustainable growth and greater market penetration yet may rely upon traditional revenue models and fixed resources,” Koppy said. “That can create pressure on the marketers who are responsible for driving awareness and consideration as well as the sales professionals who are responsible for converting leads into paid outcomes.”

The leading areas for expense change increases in the near term were:

- Cybersecurity (53%)
- IT/digital transformation (51%)
- Sales and marketing (44%)

Expense change expectations

Q: How do you expect the following expenses to change in the near term as a result of pressure from inflation?



Cybersecurity focus increases

As CFOs are investing in digital transformation, they're also spending more to make sure their new assets are protected. "As you put more of your product and service interface in a digital medium, you absolutely increase the chance that you're going to have a cyberattack," Unruh said. "They go hand in hand."

In addition to being the leading area for expense change increases in the survey, cybersecurity was the most substantially increasing area of focus for finance leaders in the fourth quarter of 2022. Forty-five percent of respondents ranked cybersecurity as a top-three area of focus, a rise of 11 percentage points over the previous quarter.

Meanwhile, for the second quarter in a row, cybersecurity risks rank among the top three challenges faced by finance leaders. With 34% of CFOs ranking cybersecurity as a top-three challenge, this area just barely trailed supply chain (35%) at the top of the challenge list.

Getting a grip on costs

CFOs remain heavily focused on controlling costs in this uncertain economy, but the survey results show that they are having success in this area.

Cost optimization remains a top priority in the immediate term, with 55% of respondents rating it in their top-three areas of focus. But finance leaders' confidence in meeting cost control goals soared to 59% from 41% the previous quarter, demonstrating that many of them have figured out how to deliver on this requirement.

Denham said that in response to the economic turbulence of the past 12 months, he sees evidence that CFOs have addressed costs in a methodical way, starting with the most important items on the P&L statement and working their way down. He said labor costs were addressed first, as the survey shows a drop of eight percentage points between Q3 and Q4 in those planning to cut headcount and salaries.

Addressing the supply chain was next, as supply chain remains the top challenge identified in the Q4 survey but experienced a drop compared with the previous quarter. Because companies need investment in digital transformation and cybersecurity to compete and protect themselves, those items often can't be cut.

"They're starting to hit some of the areas that are less urgent, and there's an opportunity to optimize costs," Denham said. "That's in professional fees and other discretionary areas that are wants versus needs."

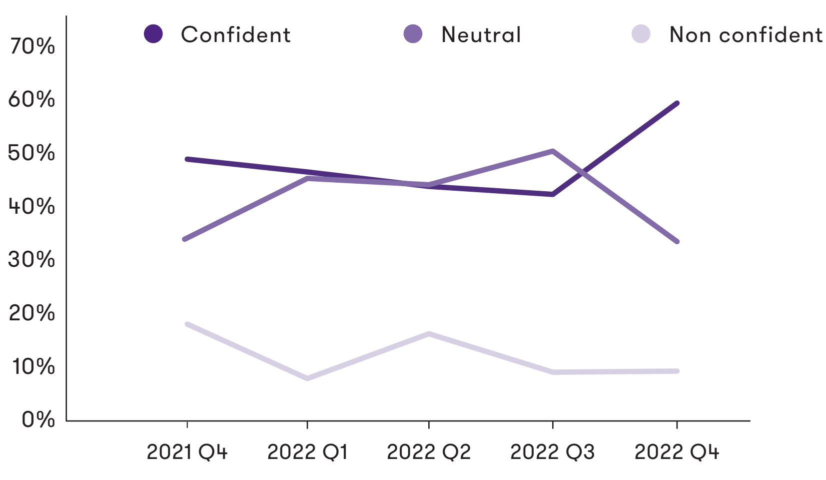
The top area for potential cost cuts is external professional consulting support and fees, identified by 45% of respondents, a rise of three percentage points over the previous quarter. Investment in long-term strategic initiatives (38%) and supplier and vendor costs (38%) also are possible areas for cuts.

In Q3 of 2022, headcount and salary were identified as the top area for cuts. But the portion of CFOs planning those labor cuts fell in Q4 to 35% from 43% in the previous quarter.

Meanwhile, the percentage of CFOs predicting a reduction in materials costs grew to 37% in Q4 from 29% in the previous quarter. After materials costs skyrocketed over the past year in a high-inflation environment, this shows a growing confidence that one of businesses' greatest challenges might be subsiding.

Getting a handle on costs

Q: Please rate your confidence concerning your business' ability to meet its goals for cost control.



Future gets brighter

Shortly after the survey fielded, there were signs that inflation may be easing.

The U.S. Department of Labor reported that the consumer price index fell 0.1% in December. While that didn't seem like a big drop, it was the largest month-over-month decrease since April 2020.

At the same time, CFOs in Grant Thornton's survey said they were growing more confident in their ability to meet their supply chain and workforce needs. With their costs also under better control, that meant a possibility of brighter days on the horizon in 2023.

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