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Synthesis

German CFOs to focus on performance and strategic flexibility after COVID-19

Highlights from 12 digital gatherings with over 250 Chief Financial Officers in Germany, hosted by Egon Zehnder

Chief Financial Officers are focusing on crisis management, future performance and strategic flexibility in the wake of the financial repercussions triggered by COVID-19, Germany's leading CFOs revealed to Egon Zehnder in recent digital gatherings.

Recent weeks have been a rollercoaster for many CFOs, who have had to deal with a multitude of topics at once, while acting as a core member of a global virtual "crisis war room" on a daily or even more frequent basis. While some found this energizing and have experienced unparalleled team spirit, it can also be "exhausting and isolating" at times, admits one CFO.

The global extent and severity of the COVID-19 pandemic means companies are facing a financial crisis the likes of which has never been seen before. "Even the lessons from the 2008 financial crisis haven't prepared companies for what is coming," says one CFO.

Some CFOs are taking a rather cautious long-term view, motivating them to take proactive measures and ready themselves for a worst-case scenario.

Others, meanwhile, have used the situation to strategically reshape and strengthen their balance sheet to take advantage of potential future opportunities.

Forecasting or fortune telling?

The problem is, nobody knows when the current crisis will end. Most experts can't even rule out a second or even a third wave of infections, which will hit the economy even harder. As a result, most CFOs don't expect the German economy to return to normal before 2022. This makes the CFOs' job incredibly difficult: how can they fulfil budgeting and forecasting requirements, without using a crystal ball, asks one?

Most CFOs have currently put cumbersome bottom-up budgeting on hold in favour of a top-down macro-factor based approach. The uncertainty ahead means they have to cater for different scenarios, ranging from an optimistic "return to normal in 2021" to a worst-case scenario of a "severe recession without foreseeable return to pre-crisis levels". Some CFOs are even consciously pursuing the worst-case scenario option as the basis for a comprehensive contingency plan that clearly defines all possible measures. Others are applying reverse scenarios and examining questions, such as "How long would we sustain our business without further revenues?" or "Which contractual obligations would we breach if production is down for another month?" CFOs want to be prepared, have all relevant approvals in place and all stakeholders aligned in order to be able to act swiftly, if necessary. "The ideal would be to have a full contingency plan prepared and in the end not to need it," declares one CFO.

There is no common industry practice yet as regards scenario analysis and guidance publications. Auditor requirements for annual accounts remain unchanged with forward forecasts expected. Emerging practice on guidance publication varies from "no guidance at all" to "guidance within a range of outcomes" or "conditional guidance". Fortunately, analysts and capital markets have reacted pragmatically and accepted the absence of guidance for the current year.

Unsurprisingly, shareholders are seeking greater reassurances right now, and requesting frequent updates, says one CFO. "Regular communication is becoming even more critical than usual as everybody wants to prevent any bad surprises." It's therefore important to be transparent about possible scenarios, assumptions and probability assessments to shareholders. CFOs who focused on digitalization in recent years are faring better, as they can draw on real-time data. For others, this has proven to be time-consuming and tedious work.

“With all the focus on contingency, it is also important not to forget long-term business viability,” says one CFO. Therefore, some areas such as R&D and important investment in future capabilities are being ringfenced and not touched in current “total cost approaches”. CFOs are communicating necessary measures to those affected in order to limit the impact on employee engagement and employer branding – after all, talent will remain a major success factor in the future.

Cash is king

The significant drops in revenue and consumer demand and upcoming changes in customer payment behaviour following the outbreak of the COVID-19 pandemic have led to a severe liquidity shortage, forcing some companies to set up “liquidity war rooms” and “cash task forces”. Moreover, re-financing and short-term liquidity acquisitions have become increasingly difficult, as capital and debt markets grow more conservative. Some currencies have dried up overnight as demand has soared, such as for US dollars, reveal CFOs.

Thankfully, German companies have fared better than many counterparts in other countries, largely thanks to government support, says one CFO, “The German government has been a front-runner in Europe in establishing support mechanisms for the industry, building on the mechanisms developed in the financial crisis.” These include selected subsidies and tax relief measures to large-scale single-company equity injections. These have drawbacks, however, including complex and time-consuming approval processes, rapidly evolving regulations and potential restrictions on dividend policies and bonus schemes – and in the longer run might impact the competitive landscape, say financial leaders.

Speeding up digitalization

The crisis has accelerated digitalization, agree all CFOs, stating that “many processes have been digitalized in no time at all, placing a question mark over former long-term IT projects and budgets”. Take annual general meetings, for example, with most physical AGMs postponed or cancelled and replaced by digital versions, which have proven to be equally insightful and sometimes easier to manage.

Meanwhile, over 90% of most companies' white-collar workforce has been moved to a work from home modus. This has, in several cases, even improved efficiency, which will definitely trigger a longer-lasting discussion on more flexible working methods, with likely repercussions on office real estate and whole site concepts, say CFOs.

At the same time, COVID-19 has highlighted the dependency of all business models on the human factor, whether consumers or employees, and this shouldn't be ignored, declare CFOs. It's providing difficulty to foster team spirit, and uphold motivation among a remote workforce and this means that managers, used to one-on-one jour fix meetings and physical team meetings, need to adopt new tools and behaviour.

New normal brings opportunity

While CFOs focus on crisis management for the present, their thoughts are also turning to what the future might hold. For a start, what will happen with the global supply chain? COVID-19 has underlined the need to nurture relationships with key suppliers and the importance of the global supply chain. Some companies, for example those with dependency of up to 70% on Asian suppliers or those with limited own value creation, have been more affected than others. Therefore, in future, we might see more regional sourcing and the insourcing of critical value creation steps, representing a clear reversal of the last decade's management strategy.

Secondly, severe financial impacts and liquidity shortages might result in new minimum capital and liquidity requirements, as well as mandatory buffers for corporates.

There's one certainty though: in the volatile world ahead, flexible, agile, and lean set-ups will enable companies to act quickly to changing circumstances and focus even more on performance, and this will become paramount, agree CFOs.

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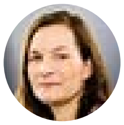

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Covid-19 Micro-Website

We have launched a micro-website where this and other informative pieces are posted. This site will be regularly updated: click here for further details.

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