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Voice of the CFO

A potential soft landing for the US economy fails to encourage CFOs

Concerns persist about economic conditions, cash-heavy balance sheets, and employment issues

As the economic factors continue to evolve, Chief Financial Officers (CFOs) are still a bit apprehensive, with many expressing that the optimism they started to feel in the recent past is being dampened by visibility challenges when it comes to the future.

Kenneth Kim, KPMG senior economist, told CFOs, "One of the changes in our outlook for the US economy is that we now anticipate a soft landing." Positive indicators he highlighted include a significant drop in inflation, a consumer price index (CPI) of 3.7 percent (9.1 percent a year ago), an improving labor market, and wages above CPI—all of which give employees more purchasing power. He noted that July's CPI report was in line with expectations and another sign that the pace of rising prices is easing. Meagan Schoenberger, KPMG senior economist, added, "We are also seeing a bit more normalization in terms of goods and services." Softer inflation readings indicate that the Federal Reserve's rate hiking cycle may be over.

CFOs seem to have a less optimistic view. A CFO in the tech industry put it this way: "If you would have told me that things were getting worse, I would have believed that narrative based on a lot of the dialogue I've heard." A CFO from a tech industry supplier added, "I think the visibility at a year level is extremely low. A case can be made for being anywhere on the curve in terms of cycling up or cycling down." For other CFOs, there are certain pockets of their business that are healthy while other areas face tough sledding or more of a normalization of market conditions.

Kim supplied the counterpoint, noting the dichotomy between US growth and the rest of the world, where economic conditions are far from ideal. "For multinationals, China's economy is experiencing deflation, which also impacts their biggest trading partner, Germany. The European economy, in fact, has been flirting with recession. The UK central bank and others may continue to tighten rates, due to higher inflation than the US, adding downside pressure on their economies. Right now, the US is looking like the best house in the neighborhood in terms of growth," among advanced economies.

Key takeaways

- The US economy is predicted to experience a soft landing, lowering fears about recession.
- Current numbers are a sign of resiliency, including easing CPI inflation.
- Economic conditions are more favorable than overseas, with China experiencing deflation, Europe in recession, and theEuropean Central Bank and Bank of England central banks likely to tighten rates further.
- CFOs are cautious, turning to tactics such as adding cash to their balance sheets and keeping an eye on credit markets.
- Although recruiting challenges are lessening in some quarters, positions in areas such as engineering and accounting remain difficult to fill. Merit increases are in the range of 3–4% for most.
- The new Securities and Exchange Commission (SEC) cybersecurity rule is less draconian than expected, lessening pressure on CFOs and others in the C-suite.

CFOs proceed with caution

Retaining liquidity: CFOs at companies that do a significant amount of international business and have global supply chains are taking conservative steps such as setting aside more liquidity, resulting in a suboptimization of their organizations' balance sheets with cash.

A global investment management company CFO said, "We're erring on the side of holding a little more, not because I think we need it, but because investors are overly focused on the softness of the number." Another CFO chimed in, "We're just trying to build in as much optimal optionality as possible."

At the same time, a steel industry CFO expressed some reservations about this approach. "The lack of visibility in our growth plans is causing us to set aside more liquidity than we're comfortable with." Others expressed concern about how long they will be able to keep cash on the sidelines when senior executives need infusions to pursue goals.

Despite reservations, CFOs are already in the midst of 2024 planning and starting to see green shoots. Some optimism goes with making smart moves like earning interest on stockpiled cash and adding real-time scenario planning to sharpen near-term forecasts.

Keeping an eye on credit markets: Another concern area for CFOs is credit markets. Kim said, "Even though we think the Fed is done raising rates, longer-term yields are determined by global market participants." If loan delinquencies continue to rise, then banks will experience continued pressure. The Fed's quarterly survey of banks found that 70 percent said they would tighten underwriting standards for commercial real estate loans.[1] Kim explained that this would likely mean more scrutiny of loan applications in addition to the impact from higher interest rates.

Third-quarter workforce trends

CFOs' views varied when it comes to evolving workforce issues, from hiring and retention to compensation and return-to-work policies.

A global investment management company CFO noted, "We're seeing a much sharper slowdown in employment growth among midsized and large companies. For companies with fewer than 500 employees and start-ups, we see relatively healthy employment growth."

The struggle for several CFOs is hiring for key roles in accounting and engineering. Failure to fill key positions can create wage pressure. "We'll almost pay whatever it takes to get people for certain roles," said a steel industry CFO.

Employee attrition—defined as a reduction in staff due to retirement, resignation, termination, or relocation—is extremely low by US standards.

When it comes to compensation, some CFOs said they offer an across-the-board three percent to four percent increase. Others are more selective with raises, offering larger increase to high performers and talent in areas with high turnover. An energy infrastructure CFO referred to his company's approach as rightsizing.

CFOs have shifted their focus to some extent from remote and hybrid work strategies to return-to-work policies. One CFO said, "Our company is about to announce a return to the office for all employees at the manager level or above, five days a week." Other CFOs are still exploring the issue and struggling with peripheral issues such as sufficient parking in smaller office spaces.

SEC's new cybersecurity rule

Many CFOs are expressing relief about the SEC's new cybersecurity rule. The original draft was more severe in its disclosure requirements, but, thanks to the comment period earlier this year, the final version of the rule is more palatable.

One issue that has been brought to CFOs' attention by chief information security officers and in-house counsel is the four-business-day reporting requirement from a material determination of an incident. Erin McCloskey, KPMG Audit partner, remarked, "Companies will need to institute required disclosure controls and procedures, and the SEC will be looking for adherence to them to demonstrate a good-faith effort to be in compliance with this reporting requirement."

Other environmental, social, and governance SEC rulemaking on the horizon relates to the human capital disclosures proposal and the climate-related disclosures final rule.

[1] https://www.federalreserve.gov/data/sloos/sloos-202307-chart-data.htm

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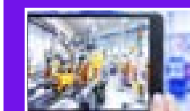

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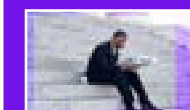

SEC finalizes cybersecurity rules

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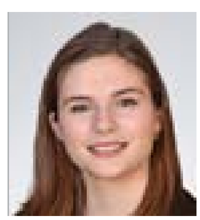

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