

C O R P O R A T E F I N A N C E P R A C T I C E

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What next? Ten questions for CFOs

As companies shift their attention from fighting the crisis to getting the most from the recovery, CFOs must keep them focused.

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The credit crisis and its shocks to the real economy have put chief financial officers on the front lines, as they implement emergency measures to help companies survive the recession. Now, as an eventual recovery begins to seem more likely, the CFO's task may become still more complex. Even for those whose companies avoided the most severe effects of the crisis, uncertainty about the future is abundant, and credit remains tight. Capital and management time are available for only a few relatively big moves, and a new appreciation of risk accompanies each opportunity.

So the CFO's judgment will be critical to push the management team's thinking on the opportunities and to cast a dispassionate eye over the costs, benefits, and risks of pursuing them. Here are ten questions we think all CFOs should be asking themselves and their executive colleagues as the recovery approaches. Read the questions and tell us what you think a CFO's priorities should be coming out of the crisis.

1. *What shape will a recovery take?* Even if the worst is over—though we make no assurances that it is—much uncertainty remains about the recovery's nature and pace. A steady recovery over 12 to 18 months would pose challenges very different from those of a tepid one over, say, five years or even a slip back into recession. What weight are you giving to the possibility of wage and price inflation, high unemployment, lower international trade, or dramatic swings in currency values? What's more, if excess leverage inflated demand and profitability in the years leading up to the crash, CFOs must help managers to understand what they should expect as normal after the crisis has fully passed and to set appropriate performance targets.¹

2. *Have you restructured enough?* A weak economy makes it easier to implement unpopular operational changes and divestitures: companies have more leverage over suppliers, unions and regulators are more cooperative, and employees understand the need for change. When the economy strengthens, these advantages will quickly vanish. CFOs should challenge their colleagues to examine how much more restructuring might be undertaken to secure a company's cost position for the medium term.

3. *Is your supply chain sufficiently flexible?* In 2008, the key question was what would happen if the downturn was worse than expected. In 2009, it's worth considering what happens if the surprise comes on the upside. An intense focus on reducing costs and working capital will leave many companies incapable of responding to a rapid pick-up in demand. Can they respond without either bringing back high costs or cutting the quality of their products? If not, CFOs should take time now to consider whether their companies may have stretched the supply chain a little too thin.

4. *Do you have a short list of acquisition targets ready?* This crisis, so far, seems to echo the experience of previous ones: equity market valuations are recovering a lot faster than economic fundamentals.² Acquisition-minded companies that wait for clear evidence of recovery before moving on attractive deals may well find themselves preempted by better-prepared competitors and miss the opportunity entirely as valuations bounce back.

5. *Should you restart conversations with potential alliance partners?* Last year, many companies put discussions about strategic alliances and joint ventures on hold. This year, if the underlying logic of those deals remains sound, many potential partners are finding themselves under greater pressure to close them. Moreover, businesses that may emerge from the recession at a competitive disadvantage could find a quick and effective solution in joint ventures with companies in a similar predicament.

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6. *Are you ready to divest newly underperforming businesses?* There's no room for sentimentality in portfolio planning. The downturn changed many industries fundamentally, and once-strong businesses may emerge from the crisis in a weaker competitive position. Divesting them now may be better than spending the next economic cycle trying to fix them. Buyers will emerge as the market recovers—and companies can free up cash for better opportunities elsewhere.

7. *Do you have the financial resources needed for an upturn?* Growth requires capital. Companies may require more working capital or have to finance the development of additional products, distribution channels, and marketing programs or the acquisition of new businesses. Credit and equity have become scarce resources, and new financing may not be timely enough to support the market's full recovery. To finance growth, CFOs should prepare a battle plan—including ways to line up new equity, as well as bonds and new debt—that can be activated if necessary. CFOs in countries where the volatility and uncertainty of the crisis have pressured the currency should understand how a recovery will affect the ability to raise capital.

8. *Have you taken advantage of the buyers' market for talent and other resources?* In a recession, most companies focus on cutting costs—head counts, discretionary marketing expenditures, R&D, product development, and capital spending. But all of these now cost less than they have in a decade, especially hiring new finance professionals. Research on previous downturns shows that the future winners made disproportionate investments in talent, marketing, R&D, and capital spending at exactly this point.

9. *Do you know what risks a recovery might bring?* Risk management and contingency planning are typically better at highlighting day-to-day issues than at anticipating major shifts. Yet an economic turnaround could bring a number of structural changes, some relatively predictable and with far-reaching effects. How well, for example, do you understand your company's exposure to major currency or commodity price movements? Do you know whether the health of channels, customers, or suppliers might create substantial structural change or whether your company is prepared to deal with high levels of volatility that may continue even as a recovery builds?

10. *Can you sell your recovery plan to investors?* Too many companies were unprepared for the downturn, lacking clear plans to communicate with investors or good answers to difficult questions from analysts. Don't be caught without a response when someone asks you what you're doing to capitalize on the upturn.

¹ See Richard Dobbs, Massimo Giordano, and Felix Wenger, "The CFO's role in navigating the downturn," mckinseyquarterly.com, February 2009; and Ian Davis, "The new normal," mckinseyquarterly.com, March 2009.

² See Richard Dobbs and Timothy M. Koller, "The crisis: Timing strategic moves," mckinseyquarterly.com, April 2009.

A few big ideas that become realities will be worth much more than a dozen that don't quite get off the launching pad. Thoughtful CFOs will ask themselves which handful of bets could have the biggest payoffs and then mobilize the bulk of their time, capital, and resources to make those bets succeed. **Q**

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