# Managing through COVID-19: Six imperatives for CFOs

Slightly more than a decade after the Great Recession, COVID-19 has brought back the dreaded "R" word to haunt executives in the global economy. The practice of social distancing to slow the contagion has abruptly and sharply curtailed economic activity around the world. Moreover, it is becoming clear that a worldwide recession of significant depth emerged in the first quarter of 2020 and may continue for an uncertain period.[1]

Downturns and recessions are challenging, but some businesses are not only able to come out intact, they are also able to seize on opportunities to outdistance their competition and position themselves for future growth.[2] Still, the speed at which the COVID-19 crisis is unfolding may likely require CFOs to use new tools—virtualization and scenario-based forecasting, for example—in addition to the traditional levers they have used to act swiftly and reasonably.

In this period of rapid economic deceleration and uncertainty, there are six distinct imperatives—outlined in this issue of *CFO Insights*—that we believe can help CFOs protect their companies and workforces:

1. **Prepare for talent disruption and virtualize your organization** by providing resources for your talent and making clear how people should support one another, and by virtualizing the finance function and other parts of the organization to operate effectively amid social distancing;
2. **Bolster liquidity** by managing short-term credit, cash, and performance needs;
3. **Communicate** frequently with critical stakeholders to keep them informed;
4. **Drive operational improvements** necessary to navigate the sharp downturn;
5. **Manage risks** and serve as stewards of company assets during this vulnerable time;
6. **Plan for recovery post the COVID-19 crisis** by strategically positioning and utilizing assets.

### Imperative #1: Prepare for talent disruption and virtualize your organization

COVID-19 requires focus on the health and well-being of your talent, as well as that of their families, given the rapid changes they could face daily. For workforce

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safety, it's important to virtualize back-office and other operations as quickly as possible. The following are steps CFOs can take to help protect their talent's well-being and support the success of virtualization:

- **Plan for critical staff who may become ill**. In a contagion, many of your key staff—or even you—may be unable to work for a period of time. In the event leaders and others are unavailable for urgent decisions and critical tasks, CFOs should consider how the chain of command and authority will shift among their staff members. From protocols for access to critical files to retasking other staff, preparing for business continuity at an unprecedented scale—while maintaining proper internal controls—is critical. As staff and their families can be significantly stressed under the current circumstances, it is also important to work with HR to provide hotlines and resources for support. Taking care of staff is a top priority.
- **Support virtualization of finance and other functions**. Shelter-in-place orders and social distancing require companies to virtualize work, and finance can likely be virtualized more readily than some other functions, such as product manufacturing or store operations. CFOs need to support this change and lead by example. Working with HR and IT, CFOs should determine ways to help their staff connect online and to elevate employee engagement overall. Virtualization of work can potentially undermine traditional sources of work satisfaction. Furthermore, discussions on ambiguous issues, usually best done in person, will have to take place virtually. Care must be taken to avoid misinterpretations in a virtual work setting where visual and other social interaction cues may not be obvious.
- **Provide IT with critical resources and funding for virtualization**. Many companies do not have systems in place for full virtual access to critical systems and data. CFOs should work with their CIOs to support essential remote access to key systems and data, while maintaining proper security of information. Staff will likely need remote training and support to help them adapt the new systems and processes to their work.
- **Minimize infection risks for staff on premises**. Some staff, especially in production and operations, will not be able to work from home. This constraint will require new ways of organizing the workspace to enable social distancing, safe handling of materials, and efficient disinfecting of the workspace. CFOs can play a key role in planning for the resources that might be needed for their companies to reorganize their workspaces.

## Imperative #2: Bolster liquidity

A foremost priority for CFOs is to ensure enough cash and liquidity for their company to operate—even more so for CFOs of highly leveraged companies. In recent weeks, the cost of financing has risen, and new stock issues through public markets have become unattractive given declines in global stock prices, market volatility, and challenges in forecasting earnings.

Central banks have authorized massive injections of capital to provide liquidity in the credit markets. Governments have also announced various fiscal stimuli to support citizens and companies through the current crisis. For some corporations, credit ratings could be downgraded due to decelerating cash flows, making new capital borrowings more expensive or unobtainable.

In this environment, CFOs should consider the following steps to secure and control liquidity, as well as manage their financing and credit rating relationships:

- **Model cash flow**. Modeling cash flow can help CFOs identify how many weeks of liquidity the company has under stressed business scenarios.
- **Revisit financing and liquidity**. CFOs and treasurers are refreshing their understanding of current debt arrangements, considering whether there might be potential breaches of financial covenants, material adverse changes, and/or cross default triggers that may compromise access to core funding and liquidity. Be proactive with financiers to seek waivers and get ahead of potential issues.
- **Centralize cash release decisions with the CFO or treasurer**. Identify the multiple places where cash may be released and prioritize which payment types and vendors are to be paid.
- **Diversify and secure new lines of credit**. CFOs may want to expand their network of banks or financing sources to secure additional lines of credit if access to new bank loans diminishes and covenants become more restrictive. In the near term, CFOs might consider taking advantage of government loans and grants, and central bank purchases of bonds to shore up their access to cash.

- **Monitor and manage receivables**. Customers and vendors generally lengthen their time frames for payment as they confront cash-flow and credit challenges. Closely managing receivables and quickly dealing with disputes can help mitigate the risk of payment defaults and delays. CFOs may need to work with credit and collections, treasury, and other finance teams daily to monitor and ensure strong cash flow and identify impacts on revenue. Conversely, companies may opt to take a larger float by extending payment terms to suppliers.
- **Work closely with suppliers**. Some critical suppliers are likely to be vulnerable to bankruptcy during the COVID-19 crisis. Business continuity may hinge on arranging alternate sources of supply, prepaying critical vendors, or ensuring sufficient credit for the supplier to continue operations. Third-party risk assessment and management will become critical over the next six to 12 months.
- **Leverage tax planning**. Tax planning can be vital to reducing cash outlays and preserving cash. Taking action in several areas can help CFOs conserve cash in the nearer term. For example, CFOs can consider repatriating cash from non-US jurisdictions, cash tax planning with respect to analyzing and filing refund claims, and accelerating deductions or deferring revenue. In addition, the CARES Act provides specific tax relief benefits intended to generate cash, such as payroll tax deferral, employee retention credits, expansion of the NOL carryback rules, and favorable changes to the business interest expense limitation rules.

Many S&P 1,000 companies entered this situation with solid growth and strong cash positions, so not all will have trouble accessing cash. Still, the contraction in demand predicted for the next two quarters may be challenging, making it critical for CFOs to manage liquidity and cash in the near term. For those faring relatively well, with strong liquidity, CFOs might consider how to help their customers and suppliers get through this crisis. Dynamic discounting of payments and supply chain financing are possible alternatives.

## Imperative #3: Communicate frequently and clearly with stakeholders

In times of uncertainty, it is especially important to have clear and frequent communications with critical stakeholders. For CFOs, this may mean daily communications across the executive leadership team, as well as with the audit committee chair and other board members, depending on the state of the company and cash flows. The COVID-19 crisis will also likely require more frequent communications with banks or private equity investors, as well as with employees. Implementing an easy-to-read format or dashboard of developments to keep critical stakeholders informed and to clarify which issues require immediate attention and which ones can be postponed, can help. Establishing the appropriate technical and communications support can also help to reduce the burdens of preparing for and executing this process.

Communicating with investors during these times is also critical. Uncertainty is the last thing that investors want, so providing them information—within regulatory guidelines—about what actions your company is taking to deal with the crisis and how they might impact performance is essential. In the wake of the COVID-19 pandemic, many companies have altered their earnings guidance. For some companies, unprecedented volatility may be an opportunity to shift away from quarterly earnings guidance and focus on long-term growth.

Regulators are another key stakeholder to communicate with at this time. Over the last several weeks, regulators, including the SEC and PCAOB, have issued statements related to financial reporting and related financial statement disclosures. On March 25, 2020, the SEC issued an "Order" extending certain filing deadlines. "Health and safety continue to be our first priority," said SEC Chairman Jay Clayton in a public statement. He continued, "These actions provide temporary, targeted relief to issuers, investment funds, and investment advisers affected by COVID-19. At the same time, we encourage public companies to provide current and forward-looking information to their investors and, in these uncertain times, companies are reminded that they can take steps to avail themselves of the safe harbor in Section 21E of the Exchange Act for forward-looking statements."

Registrants that are concerned that COVID-19 could negatively affect their financial reporting quality or ability to meet the modified SEC filing deadlines are encouraged to proactively reach out to their auditors, legal counsel, or the SEC, as appropriate, to consider the availability of additional relief. In addition, registrants may wish to consult with legal counsel regarding how reliance on the Order may affect their access to capital markets.

Many private companies also have concerns with respect to filing their financial statements to satisfy bond holders' and others' requirements. Again, they should seek guidance from regulators.

## Imperative #4: Drive operational improvements

Beyond virtualization, both finance and business operations will have to adjust and step up to address changes in demand during the current crisis. Consider what needs to change in how the company operates and what opportunities can be seized during this time. Some critical steps CFOs can take include the following:

- **Shift forecasting models to scenarios**. The rapid deceleration of business will make forecasting near-term revenues and earnings challenging. Existing forecast models based on normal work and in-person interactions may no longer be valid. CFOs will have to drive scenario planning to guide revenue and cash flow forecasts, plan for capital utilization and management, and create optionality. Modeling capital expenditure should focus on the timing and size of investments needed to position the enterprise for a rebound and competitive advantage, as well as on weighing how much certain reductions could hurt competitive positioning. CFOs should also consider establishing a cross-functional SWAT team—composed of stakeholders from within, and external to, their organization—that can help understand and identify the inputs that will be critical for scenario planning.

- **Reduce enterprise costs**. Given the severity of the drop in demand and the need to preserve cash, many companies have already begun enterprise cost-reduction initiatives. SG&A and procurement are two areas where companies can reduce costs and gain efficiencies. The COVID-19 crisis also provides an impetus for restructuring and consolidation to achieve efficiencies, such as moving to a virtualized shared services model. Judiciously executed outsourcing contracts can allow companies to shift high fixed costs to variable costs that can adjust with trends in the economy. As future corporate real estate needs may fall due to an increase in working remotely, there may be opportunities to reduce leased space and sell assets.

- **Rationalize and diversify procurement**. Given the impact of COVID-19 on supply chains, this may be a time to diversify supplier sources and lock in critical forward contracts. CFOs potentially have the opportunity to drive new bargains across asset categories, from raw materials to real estate. During this unsettling period, it also may be a time to buy options and forward contracts at low prices, but doing so will require careful consideration of suppliers' ability to survive the pullback created by the COVID-19 crisis. For US buyers, the dollar has strengthened against many currencies, and commodity prices have dropped substantially.

- **Improve pricing discipline**. Price execution at many companies is decentralized and inconsistent across salespeople and customers. A downturn provides the opportunity to catalyze and execute a rational pricing and organizational strategy. Consider that a 1% increase in price can yield upwards of 10% in operating profit in many cases. Generally, stronger discipline around pricing can also help protect against the downside, as customers put greater pressure on margins during a severe downturn.

- **Rethink the portfolio of assets**. Depending on the duration of the crisis, some companies may not be able secure enough cash to ride it out long-term—possibly forcing them into bankruptcy, restructuring, or liquidation. CFOs need to immediately consider what assets they will dispose of and how to structure their portfolio to best survive and maintain value. For companies with strong balance sheets, this could be an ideal time for strategic acquisitions. Asset values have dropped considerably, and highly leveraged targets have become more vulnerable, so new opportunities accretive to earnings could emerge for acquiring companies. Prior to the COVID-19 crisis, many companies accumulated cash, and the dearth of M&A candidates at affordable valuations often resulted in cash being returned to investors through share buybacks or dividends.

### Imperative #5: Manage risks

In addition to their financial duties, CFOs will have to keep a sharp eye on risk management and stewardship. Some direct risks to manage include the following:

- **Internal controls and fraud**. As layoffs and cost reductions occur, companies could become increasingly vulnerable to failures of internal control, given stretched, disengaged, or ill staff. CFOs should be especially vigilant about fraud, as these failures can add substantial costs.

- **Supplier and customer failures**. As discussed earlier, downturns and recessions, in general, can disrupt supplies or receivables. Diversifying and securing suppliers and monitoring customer payments can help mitigate these risks. Third-party risk management remains critical.

- **Cyberattacks**. As companies virtualize their workforce and create more external access points to their systems, they potentially become more vulnerable to cyber risks, including data theft, ransomware, and other attacks. Vigilance and investment in cybersecurity will continue to increase in importance.

At the same time, companies will face indirect risks in the global economy that can have severe impacts, depending on the duration and depth of the contagion. For example:

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- **Failure of policy interventions**. Governments and their central banks are injecting massive amounts of cash into their respective economies to stimulate demand. However, it is unclear whether the moves will be enough to offset unemployment or whether they will work to stimulate and reignite demand in the economy while many individuals must shelter in place. Furthermore, it's uncertain whether the moves will be sufficient to instill confidence in investors in a timely way to provide credit and liquidity in markets.

- **Cascading risks**. In our first "value killers" study of risks that led to major drops in companies' valuations following the Great Recession, we found that one risk often led to another interdependent risk. In our hyperconnected global economy, investors are beginning to understand critical interdependent risks that can be activated by the slowdown stemming from COVID-19. For example, could governments' borrowing to provide stimulus trigger national debt defaults that cascade through the financial system? Could governments of heavily indebted countries face limited access to liquidity?

Given the uncertainty of the depth and duration of COVID-19 and the related economic impact, we do not know what cascading risks will emerge over time. CFOs will have to continuously engage in scenario planning to identify which risks are most likely to impact their company. Still, there will be risks that cannot be foreseen or easily mitigated, requiring liquidity and agility to respond.

## Imperative #6: Plan for the recovery

Although it's uncertain when the economy will start to recover from the impacts caused by COVID-19, it is not too soon to think about your organization's future plans. As social distancing makes this crisis unique, CFOs should consider exploring different recovery models to determine which markets and segments could bounce back first. The analysis can help in focusing investments and developing plans to respond to the recovery. Such plans may include acquiring or maintaining specific assets that could bolster an organization's recovery. Other options might include the following:

- **Filling critical talent needs**. In general, economic downturns and recessions often result in layoffs, furloughs, and downsizing. Yet, companies will likely continue to face the long-term talent shortages they have experienced in recent years, especially during and after the recovery. A downturn presents an opportunity to hire critical talent from other organizations and universities that may be forced to downsize as they deleverage. Campus and experienced-hire recruiting may also yield more qualified candidates at lower prices over the next two years.
- **Selective product and service innovation**. During drastic downturns, as well as recessions, research and development (R&D) can suffer, but too much paring back can undermine the delivery of future products. When we analyzed high-performing companies that navigated prior recessions, we found that most continued to innovate, introduce new products, and position products and services for growth. The current crisis provides an opportunity to focus R&D on the products, services, and packaging likely to be most attractive over the next several months and after the crisis has diminished.
- **Digital transformation**. Many companies were already undertaking digital transformation initiatives before the COVID-19 crisis struck. With the virtualization of work and the possibility of its continued use, sustaining efforts to virtualize the workplace and operations may help companies better meet future needs. After the COVID-19 crisis has abated, many consumers are likely to engage more in e-commerce, and people may prefer to continue working remotely. When managed well, virtualizing how and where people work could lead to improvements in productivity, as well as increased customer and workforce engagement.
- **Decoupling and creating resilient supply chains**. The pandemic exposed the vulnerability of supply chains, initially to China and later to other countries. Consequently, companies will likely take steps to reconfigure supply chains to be more resilient to future disruptions. Such steps could include more onshoring and "nearshoring" of production, greater automation, and using additive manufacturing to create new supply chain options.

During economic downturns, it's natural to focus on cost-cutting; however, by staying the course on initiatives that support long-term growth, CFOs can play a critical role in financing and positioning their companies for recovery.

## Where to now?

Outside of China and Italy, the COVID-19 crisis is in its early stages. Different geographies are likely to recover at varying rates, based on the availability of health care and containment of the COVID-19 contagion. As of the time of this writing, some[3] observers seem to point toward a V-shaped recovery, starting in two quarters, although much uncertainty remains.

Given the uncertainty, CFOs should develop strategies to navigate the COVID-19 crisis, using scenarios of different depth and duration. Planning should consider a range of scenarios from worst case to best case, taking into consideration talent, operations, suppliers, customers, and other key stakeholders, and the possibility that COVID-19 could persist for an extended period and cascade to create other risks.

CFOs in companies with a strong balance sheet and cash reserves are likely positioned to seize opportunities to innovate, outdistance their competitors, and grow more quickly in the ensuing recovery. Yet, the duration and depth of contagion will likely drive the recovery. Ultimately, an effective vaccine and treatment protocol will provide the greatest benefit to secure the health of societies across the world *and* restore individual and investor confidence.

# Endnotes

1. The U.S Department of Labor released the unprecedented seasonally adjusted weekly unemployment claims of 3,283,000; https://www.dol.gov/ui/data.pdf.

2. Kambil, Ajit; "What is your recession playbook?" Journal of Business Strategy, Vol 29, No.5, pp. 50-52, 2008.

3. Hatzius, Jan, et al., US Daily: A Sudden Stop for the US Economy, Goldman Sachs, March 20, 2020; https://www.goldmansachs.com/insights/pages/gs-research/us-daily-20-mar-2020/report.pdf.

***For more information on how CFOs and other C-suite executives can respond to the current crisis, visit the dedicated COVID-19 site on Deloitte.com.**

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