Voice of the CFO

As economic uncertainty persists, CFOs are approaching forecasting with agility and, increasingly, artificial intelligence

KPMG LLP (KPMG) convened a cross-industry group of chief financial officers (CFOs) to talk about current economic realities, the complexities of forecasting, and how technology and talent strategies can help alleviate some of the pressures. Sanjay Sehgal, Advisory principal and head of Markets, who led the discussion, was joined by Kenneth Kim from KPMG Economics and Brianne Lumley from the firm's Human Capital Advisory practice.

The economy is a moving target

The session kicked off with an overview of current economic trends by Kenneth Kim, KPMG senior economist. The nation is at 3.4 percent unemployment, the lowest rate since the 1960s, and half a million new jobs were created in January. Although retail sales during the holiday season were weaker than expected, they bounced back in January and are expected to continue to improve in 2023, which is partially attributable to record Social Security payments. According to Kim, "Although consumers had $2.2 trillion in savings they amassed at the height of the pandemic, they still have $1.1 trillion in excess savings, which should act as a near-term tailwind to spending."

Kim's views were supported by the perspectives the CFOs shared.

One CFO said, "The balance sheet built up during COVID has kept the consumer strong. However, there is a discernible dichotomy between wealth levels. Those with higher income are more likely to still have savings while lower-income households have depleted stimulus funds more quickly." Kim added to this view by stressing that, in the bottom 20 percent of income distribution, people are struggling. This trend started in the middle of 2022 with high inflation rates and now people are defaulting on auto loans and checking account balances are eroding to levels akin to the 2008–09 financial crisis. "More people in the lower-income distribution are living paycheck to paycheck," he said.

As far as inflation and potential recession are concerned, Kim said that the Federal Reserve (Fed) is currently planning to go higher and longer with interest rate hikes until at least the summer. "We thought they'd be done by May and only raise rates as high as 5.25 percent," he said. "However, now we think they will go as high as 5.75 percent by the summer."[1] He continued, "As to where this ends, a new term has been coined—'no landing'—to indicate that there will be neither a hard nor a soft landing and the economy is unlikely to see a recession."

Key takeaways

- Despite economic uncertainty, consumer spending remains strong, although higher-income families have retained more of their savings than lower-income families.
- Spending has shifted toward services and experiences and away from material goods, particularly technology products.
- CFOs are largely still optimistic about avoiding a recession, although concerns remain around how much longer the Fed will continue to raise interest rates.
- Forecasting and communicating with the board of directors require exceptional flexibility, regular communication, and some use of predictive analytics as the economic outlook remains a moving target.
- CFOs are pushing for adoption of artificial intelligence (AI) and advanced data analytics not only to improve forecasting, but also to alleviate time pressure faced by the current workforce.

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A split between spending on goods and services

While some CFOs in the consumer goods sector are noting a slowdown in spending, those in service-oriented industries, such as restaurants and other hospitality sectors, are seeing sustained activity.

A semiconductor CFO noted a softening of the market for technology products, as consumers likely already have "all the TVs, PCs, and phones they need." In contrast, a hospitality industry CFO said that they are seeing more consumers spending money on services and experiences than they saw three years ago—before the pandemic. "There hasn't been any erosion on the traffic side," they said. "And we aren't seeing what we call 'check management,' like not ordering appetizers or dessert."

One CFO summed up the outlook on spending by saying, "While we have concerns around the health of the consumer, the strength of the labor market means the consumer isn't rolling over yet."

This view was echoed by a food industry CFO who highlighted that they had to account for the fact that a large portion of their business is commodity driven. "Conditions can be steady for years and then we will see a quick price spike in China. In our ecosystem, we need to focus on the top 10 to 15 issues we can manage within certain parameters."

A CFO of a company that manufactures capital equipment for energy companies concluded the discussion on forecasting by saying that they provide base-case scenarios to their Board and try to think through longer-term projects with the understanding that the outlook can change very quickly and drive the need to make course corrections. "We provide the upside, but we spend more time thinking through downside scenarios related to capital structure, allocation decisions, and planning," they said. "Still, to drive efficiency, speed, and consistency in the forecasting process, we are strengthening our FP&A processes and using codified templates and data structures."

The key to forecasting today is agility

Sanjay Sehgal led a discussion around how companies are approaching forecasting, posing a question about whether Boards are comfortable with the need for CFOs to present flexible scenarios given fluctuating economic conditions.

In response to a food industry CFO saying that they were seeing great progress in their AI pilots, they added that pilots aren't that difficult to do and that "the true challenge is redesigning organizational structures and processes and accessing talent to tap the full value of AI."

A natural gas CFO stressed that their forecasting was changing every three months in line with the changing economic outlook. "We need to be flexible, although we are fortunate that most revenue is contracted in the near term," so they have relatively good visibility into cash flow for the next year or two in at least two-thirds of their business.

An insurance industry CFO said that while they have a lot of certainty around revenues since they know what premiums are coming in, there is a considerable degree of uncertainty around costs, such as how much it costs to repair a vehicle. "The approach we are taking with the Board is to split our annual plan into two halves of the year," they said. "The first half is locked, relatively speaking. However, for the second half, we need to make some assumptions and remain agile on what levers we will pull based on what we see from an underlying profitability perspective. For example, we are planning for what we will do if policy growth decreases."

A supply chain CFO offered an alternative approach to managing Board expectations around forecasting. "Our typical approach with the Board is quantitative scenario planning based on growth expectations and margins," the CFO said. "However, the pandemic and now the economy have created a further grind where we have to do low-side and high-side scenario planning."

The future of forecasting will depend on AI

Sanjay Sehgal and Brianne Lumley from the KPMG Human Capital Advisory practice transitioned the discussion into the use of AI and machine learning not only for forecasting, but also throughout the business. "In finance, you are sitting on tons of internal and external data," Sehgal stressed. "The challenge is harnessing it and managing it in a creative way. There is a huge opportunity to leverage AI and digital technologies to drive improved forecasting. I believe that this is our future."

A pharmaceutical industry CFO said they have started to use AI for predictive forecasting, although they started with their highest-selling products first and are now rolling out the approach for testing in every country around the world. "Building the model is the easy part," the CFO said. "The conversations with the business to get them to trust the data is the harder part. We are just entering the change management phase."

Another CFO expressed concern about introducing these technologies without workers trained to use them correctly. "I worry about people taking action on AI forecasts without thinking about it," the CFO said. "AI can be useful for trend analyses, but it can lead to catastrophic errors in responses to big market dislocations and Black Swan events. Right now, I don't think AI is better than humans."

Regarding what the introduction of AI and automation means for the workforce, most CFOs agreed that, in the short term, these tools would supplement human capital and allow them to spend less time on mundane tasks and do more meaningful work. However, in the longer term, there was consensus that these technologies would eventually replace the need for some roles within the workforce.

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Regarding the future of work, Bri Lumley highlighted the value of CFOs partnering with CHROs to think about the future of work—post AI or technology implementation. She stressed that early partnership with CHROs is key to creating a more agile organization and understanding the skills and roles needed to shape the organization going forward.

One CFO stressed how critical it was to be mindful about messaging to employees and the human impact of some of these changes, shifting the conversation from the kinds of work that will no longer be needed to the new, exciting, and strategic work the workforce will have the opportunity to do in the future.

Sanjay Sehgal drove home that, on AI, there is "no easy answer. We are all figuring it out. Even if the technology yields 75 percent to 80 percent accuracy, the remaining 20 percent requires humans to make judgments and adjustments. We are going into uncharted territory, but the value of AI will become clearer over the next year or two."

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[1]The future path of Fed policy will be fluid as a result of financial market events that occurred the week following this CFO discussion on March 1.

Editor's note: These comments reflect KPMG insights on a fluid and uncertain situation. Our perspective may change as developments evolve. Visit KPMG Economics to stay current on KPMG commentary regarding the economic outlook.

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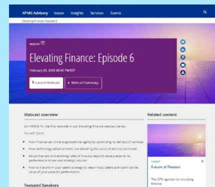

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