What Will Emerge in 2014?

The CFO as financial strategist will take on heightened importance.

By Ramona Dzinkowski

Emerging from a five-year period of relentless emphasis on risk and cash management, the focus for senior financial executives in 2014 is on revenue growth. Although CFOs haven't lost sight of the impacts of potential rising interest rates and currency volatility on their costs and revenue streams, capitalizing on a slow, yet promising recovery in the United States is the theme of the year. Meanwhile, keeping close watch on the possibility of increasing healthcare costs—and the ongoing destabilizing effects of potential government shutdowns, also known as fiscal cliff-hanging—is on the agenda once again.

Regulation and Standards

Over the next year, the major standards setters and regulatory agencies are expected to finish what they started, adding in no small way to what will be keeping CFOs up at night in 2014.

For many public company CFOs in America, and those from interlisted companies based in Canada, this means that conflict minerals disclosure will be top of mind until their first reports are filed with the U.S. Securities & Exchange Commission (SEC) in May. This initiative follows the SEC's 2012 final rule on conflict minerals, which requires companies listed in the U.S. to disclose their use of conflict minerals manufactured in the Democratic Republic of the Congo (DRC) and adjoining countries to ensure the minerals they use in their products haven't financed illegally armed groups engaged in the Congo's war. (For more details, see "What's in Your Company's Products?" in the July 2013 issue of *Strategic Finance.*)

Maximizing revenue and keeping a close watch on emerging opportunities will top CFOs' list of things to do in 2014.

A December 2012 study by Sustainalytics.com reports that companies in the sectors of information technology (IT), telecommunications, automobiles and auto components, medical devices and equipment, aerospace and defense, electrical equipment, consumer durables, and conglomerates have relatively high exposure to this type of disclosure legislation. So, yes, that covers a *really* wide swath of the global economy. (The full report is available at www.sustainalytics.com/sites/default/files/conflictmineralsreport_december2012.pdf.) It's anticipated that the rule will affect approximately 6,000 issuers in the U.S. alone (including hundreds of Canadian companies), and each will be responsible for reporting a description of the due diligence measures performed on the conflict minerals' source and chain of custody, following a recognized framework (most likely the one produced by the Organisation for Economic Co-operation and Development (OECD)); a description of relevant products that aren't conflict-free; identification of the facilities used to process the conflict minerals; and the efforts undertaken to determine the specific mine or location of origin.

Other Changes

Also in 2014, four major Memorandum of Understanding (MOU) projects of the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB)—leases, revenue recognition, financial instruments, and insurance contracts—will likely come to a close, harmonizing these standards between International Financial Reporting Standards (IFRS) and U.S. Generally Accepted Accounting Principles (GAAP). To this end, final standards and new exposure drafts will be issued, and CFOs are encouraged to review the implications of these changes as soon as possible. As Bob Herz, former chairman of the FASB, explains, these standards will affect companies in many ways. For example, with regard to the new revenue recognition standard, he says, "It's important for companies to look at their contracts and sales arrangements and figure out how the standard may affect their accounting for revenue transactions. They've got until 2017 to implement it, but for some companies it could mean a significant change.

"Also, there will be new disclosures," he cautions, "so it will be important to think about how to get the information that will be needed. Similarly, for the joint leasing project, if the Boards start to make it clear that they're going ahead with the final standard, this will require all leases over a year old to be put on the balance sheet. Consequently, there will need to be very significant data gathering on that, and that will take time." As for the U.S. allowing domestic filers to adopt IFRS this year, the SEC isn't expected to move on this in the near term.

In addition to emerging standards in 2014, CFOs can also look for the release of further proposals around how ratings agencies are selected in America, with the potential for a tough centralized system administered by the SEC. Given the momentum toward harmonizing securities regulation between Canada and the U.S., this could have spillover consequences for rating-agency regulation in Canada as well. Meanwhile, across the pond, European CFOs are waiting for final rules on auditor rotation, which most likely will require companies to change auditors at least every 20 years. (The current average is 25.) You might recall that the U.S. Congress "outlawed" the Public Company Accounting Oversight Board (PCAOB) from imposing mandatory rotation in America—*forever.*

spend more in North America as of late last year, and more recently in parts of Europe."

Moreover, CFOs are expanding their scope when it comes to forecasting revenue potential, then aligning their budgets accordingly. "In a post-2008 economic environment," she adds, "I look at things with an outside lens, such as where the opportunities are in the end-user market. I then make sure we're agile in terms of redeploying resources into that area. More specifically, as demand grows for social networking, e-commerce, or big data applications, there's a demand for increased connectivity, which in turn is increasing demand for our equipment and services."

When it comes to evaluating risk in new markets, Denholm explains that understanding potential volatility within regions has become a focal point of Juniper Networks' risk management process, particularly as it relates to supply chain management. "As part of our ongoing review of risk, like many other companies in today's environment, we look at the overall market landscape—from both an economic perspective and a geopolitical perspective," she says. "Clearly, instability in any part of the world, like what might happen in the Middle East, is something we examine in terms of scenario planning. We also look at things like M&A trends and what's happening in terms of consolidation, either in our industry or within our customer base."

At the same time, CFOs everywhere will be encouraged to review two evolving reporting and control frameworks, namely the final version of the revised Committee of Sponsoring Organizations of the Treadway Commission (COSO) *Internal Control—Integrated Framework* (issued May 2013) and the *International Integrated Reporting Framework* of the International Integrated Reporting Council (IIRC). It's hoped that the 2013 COSO framework will help organizations design and implement new internal controls to better reflect changes in business and operating environments. The revised Integrated Reporting Framework, on the other hand, is expected to propose a more cohesive and efficient approach to corporate reporting so that investors can more accurately gauge a firm's capacity for creating value over the short, medium, and long term.

Beyond Compliance and Control

Against this backdrop, CFOs will be expected to be the guiding hand around risk management, internal controls, treasury/cash management, mergers and acquisitions (M&A), and cost and efficiency management, not to mention assuming the role of corporate strategist. Yet however broad this purview may be, maximizing revenue and keeping a close watch on emerging opportunities will top CFOs' list of things to do in 2014.

Demand Driven Growth

Juniper Networks, an international provider of network infrastructure technology and services, is expecting to do a robust business in 2014, which could be part of a larger, positive trend for the global economy. Chief Financial and Operations Officer Robyn Denholm says, "We've started to see telecom equipment and service providers

Expansion through Acquisition and Innovation

For Brookfield Asset Management, a global asset manager with 23,000 employees in 100 locations, its defensive strategy of more conservative management, which saw the firm through riskier times, has turned to offense, with a more aggressive growth and acquisition strategy. Among its $180 billion of real assets under management, Brookfield owns 131 office buildings, 175 shopping malls, 19,800 apartment buildings and condominiums, 200 hydroelectric dams, as well as toll roads, gas pipelines, wind farms, and even a railroad.

As Brookfield CFO Brian Lawson explains, "Going forward, we're very focused on expanding the amount of capital that we manage for our clients. We're also focusing on acquiring new assets through Brookfield Property Partners, which focuses on commercial real estate properties, largely office and retail but also industrial and multiresidential." That strategy is directly related to continued improvement in the U.S. economy, particularly in relation to the home building sector, notes Canada's CFO of the Year for 2013.

"We've put a lot of money to work over the past three to five years in that sector, at very attractive pricing, and we're seeing earnings picking up significantly. We're expanding our reach in America, and increasingly in the Middle East and in Asia, and to a certain degree in Europe," he says.

With growth comes the need to manage an ever-wider span of projects and people while streamlining operations. "For the coming year, we're definitely continuing to invest in technology to increase efficiency," Lawson adds. "In particular, what we're really trying to accomplish over the coming months is to make sure that people have access to the right information quickly and consistently, and [that] matches our strategy across the organization."

What we're really trying to accomplish over the coming months is to make sure that people have access to the right information quickly and consistently.

Similarly, at National Instruments (NI), a global provider of hardware and software solutions for the scientific and engineering communities, one of the company's underlying tactics for profitable growth revolves around streamlining efficiencies in its global communications network. As CFO and COO Alex Davern comments, "We're always looking to leverage new technologies to drive the efficiency of our business." More specifically, to increase the possibility for collaboration and education for the company's 7,000 employees, particularly in regard to sales and marketing, NI is maximizing the potential of cloud technology. "Just the simple availability of Web content, our ability to communicate messages directly from the CEO, our ability to train our employees on our tools and technologies as we bring them to market, and line up materials for collaboration—there's an explosion in possibility there," Davern says. "And we, like many other companies, are trying to find the best, most optimal ways to tap into that."

Equity Financing, Partnership, and Investing in New Technologies

For many smaller private companies, the focus on revenue growth is fueled by many factors, including a sustainable rebound in the U.S. automotive and housing industries, job creation, increased global competition and industry consolidation (resulting in declining profit margins), and the need to attract capital. For Hamilton Specialty Bar, a private equity-backed company producing specialty steel products with primary markets in Canada and the U.S., all of the above apply. As CFO Fred Burke explains, "Since 2008, our industry has been impacted by increasingly lower spreads between the selling price and the price of scrap metal, which is the primary component of making steel. We've also seen some increased pressure from manufacturers in the Far East, specifically within the rolled flat steel market. Manufacturers that become more competitive in flat steel look at investing in higher-margin specialty steel, which increases pricing pressure in the specialty market. This, combined with an increasing number of consolidations, means there are very few smaller players left."

Burke defines his job of CFO as a value creator. "What we're going to be focused on in the coming months is improving operating efficiencies in our plant and potentially expanding our product range so we can be even more price competitive in the market and establish new partnership opportunities," he emphasizes. "This in turn will allow us to attract new financing to invest in growing the business, which will help improve our plant efficiencies, drive profitability, and build a new customer base." What risks does Burke foresee in 2014? As in many industries, it's the competition for scarce resources around the globe. "Our risks involve the growing demand for North American scrap," he says, "which increases scrap prices and further reduces our margins."

Compliance, reporting, and control will clearly remain common themes for CFOs this year. Nevertheless, the CFO as financial strategist of the organization will take on heightened importance as CFOs everywhere maintain a sharp lookout for growth opportunities while keeping the associated risks solidly in their peripheral vision. **SF**

Ramona Dzinkowski is a Canadian economist and business journalist. You can reach her at www.dzinkowski.com.