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EXPERT

Andrew Harding explains what steps finance leaders should consider to future-proof their companies as they face the growing inflation.

EVER SINCE ITS INCEPTION 31 YEARS AGO, ONE OF THE MOST FUNDAMENTAL FUNCTIONS OF AMCHAM HAS BEEN TO MAINTAIN PLATFORMS FOR SHARING PROFESSIONAL KNOWLEDGE AND EXPERIENCE BETWEEN ITS MEMBERS. THERE ARE SEVERAL SUCH PLATFORMS, INCLUDING AMCHAM MONTHLY MEETINGS, THE AMCHAM COMMITTEES, AND THE EXPERT SECTION OF THE CHAMBER'S MAGAZINE.

EXPERT Business leadership

INFLATION BUSTERS

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Strategies for combatting rising prices

How much should organizations be concerned about inflation? With the support of their finance teams, businesses must start planning for their future now to cope with the uncertainties of tomorrow's new business environment.

In July, Poland recorded its highest consumer price inflation in a decade, reaching 5 percent compared to the same period last year, according to a flash estimate by the country's Central Statistical Office (GUS). The new figure marks the highest inflation level since May 2011, when the same rate of 5 percent was recorded. This might create additional pressures for the country's damaged economy and businesses, which are struggling to survive.

UNCERTAINTIES OF TOMORROW

Economists explain that this inflation rate is being driven primarily by rises in food, energy, and fuel prices, which increased by 3.1 percent, 5.3 percent, and 30 percent year on year according to GUS's estimates. In light of the data from the European Union's statistical office Eurostat for June 2021, this was the second-highest increase in the entire European Union, just behind Hungary.

Economists say that Poland may end the year with an inflation rate of 5 percent. This would pile more pressure on the country's central bank, the National Bank of Poland, to raise interest rates—which have been kept at 0.1 percent since May 2020— in an attempt to prevent inflation from getting out of control and hampering Poland's post-pandemic recovery. Meanwhile, uncertainty remains, and we cannot rule out further Covid-19 restrictions later this year. That is why businesses must future-proof their organizations and become resilient by design now.

MITIGATING INFLATIONARY PRESSURES

Businesses fail not only because they are unprofitable in the short term but because they suddenly run out of cash. This can happen for a variety of reasons, including poor working capital management, such as inventory obsolescence or bad debts, or the loss of funding, such as bank loans or bond redemptions. Businesses also fail because of the increased cost of capital, such as higher interest rates or the need to maintain healthy dividends. For businesses facing inflationary pressures, cash reserves can serve as a buffer. In other words, cash makes a business resilient.

As business leaders look forward to the next 12 months, they should ask themselves some key questions: When planning for the future, have you run different scenarios for your business? Have you run scenarios that include your business operating in adverse conditions? Can your business survive such shocks? And if your business experiences hardship, how can it continue to generate a healthy free cash flow?

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PRACTICAL APPROACH

One of the many things I value about my role is hearing the differing perspectives of our members, who are based all over the world. Recently, I was interested in some insights our members in China provided since they have a lot of experience managing growth in an inflationary environment. As it is a growing concern for finance professionals elsewhere, they shared several practical suggestions to mitigate inflation risks. In a nutshell, they can be summarized as follows:

- Use hedging strategies to complement procurement. Hedging strategies mitigate the risk that commodities and other raw materials suddenly skyrocket in value and affect a business's profitability.
- Increase the prices charged to customers. Higher prices help to offset the impact of rising commodity prices on profit margins. Companies with a strong market position are particularly well placed to do this and should take advantage of that position. Ideally, price rises should be small but frequent.
- Renegotiate terms with suppliers. This is a particularly good option if the business is growing and has ever-larger contracts to offer.
- Be innovative. Find opportunities to reduce the cost of the goods or services your business provides — perhaps by using fewer components in a product or simplifying packaging. Also, find new channels to engage with customers — try connecting through social media rather than by hosting face-to-face events.
- Look for ways to reduce fixed and variable costs. An obvious option is to downsize office space and encourage more home working so that people are not in the workplace full time. Also, minimize travel costs by using video-conferencing tools. Applying digital technology can improve the efficiency of manufacturing and service processes.
- Drive revenue growth. Higher revenue helps minimize the impact of inflation on salaries as long as other strategies are also applied to protect profit margins, such as managing supply-chain costs and passing on price rises to consumers.
- Focus on sustainability. Sustainability initiatives can potentially help buffer companies from the negative impact of inflation. Becoming more energy-efficient is a way to reduce costs. Companies may also be able to sell any carbon credits they generate on a carbon trading market.