



Strategies & Trends in Capital Allocation

MANUFACTURING

Updated February 2022





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Now Trending

- **As companies ponder a post-pandemic future, focus returns to growth**
 - “Cash is the lifeblood of all businesses. The more working capital on hand, the greater the opportunity to spend it on strategic growth, generating lasting business resilience.” – Mark Partin, CFO, BlackLine.
- **The new mantra is "agility"**
 - With ongoing supply chain volatility, rising inflation, labor shortages, and increasing attention to ESG, the need for agility is paramount.
 - New technology investments are considered essential to said agility, and as a driver of growth. One survey conducted by KPMG revealed that a top operational priority among large enterprises is to invest in the "digitization and connectivity of all functional areas."
 - In some countries, such as Japan, companies are taking a "lighthouse approach" to accelerate digital transformation by choosing a pilot factory or process and radically digitizing operations before rolling out to other factories once proven.
- **Supply chain disruption provides challenges *and* opportunities "**
 - Though once content with "just in time" manufacturing and offshore sources, companies have starkly recognized their vulnerabilities – calling into question their planning, procurement, storage and delivery mechanisms. As a result, according to one study, "nearly 75% of manufacturers have found alternative suppliers for some inputs; however, 88% are still experiencing longer than usual leads, and 83% delaying orders."
 - Creating supply chain resiliency is accelerating interest in capabilities-driven acquisitions, new means of achieving economies of scale, vertical integration and operational consolidation.
 - "Near-shoring"/on-shoring are gaining interest as buffers to geopolitics and international supply chain disruption.

SOURCES: StrategicCFO360 – *Where CFOs Are Investing Resources In 2022*, KPMG, *Global Manufacturing Prospects 2022*, Resources & Insights, *2022 Business Outlook Trends for Manufacturing*



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- **Supply chain challenges/opportunities (cont.)**
 - "Just-in-case" stockpiling is another strategy companies are using. Accumulating raw materials and key components safeguards their production schedules.
 - As businesses look to invest in new production facilities to meet unfulfilled demand and provide more supply chain resiliency, it creates an additional opportunity to demonstrate and or initiate ESG-focused initiatives.
 - Companies that masterfully manage supply chain risk can realize a significant competitive advantage – something board directors are paying attention to.
- **Inflationary pressures loom large**
 - “Many CFOs responded to price inflation by passing on costs to customers but failed to make long-term structural changes, such as investing in suppliers to increase capacity and improve costs. The result is they are now faced with eroding margins as they pay higher prices for materials and services as demand has surged.” [Forbes]
 - Borrowing costs for businesses remain at historical lows, though long-term interest rates are now edging up. Companies generally have cash and financing capacity, though some sectors impacted by the pandemic will have difficulty funding capital spending.
 - A casualty of rising prices is the cost of equipment – which is reported to have increased 6% compared to +/- 2% in the past. Another challenge: long lead times for equipment due to supply chain issues and a shortage of labor.
- **Rising raw material costs**
 - According to a study conducted by *Resources & Insights*, 87.1% of respondents cited rising raw material costs as their primary business challenge. These manufacturers expect raw material costs to rise 6.5%, which is down from 7.5% last summer but nonetheless elevated.

SOURCES: Wipfli, *Our 2022 outlook for the manufacturing industry*, Mendix.com, *Manufacturing Outlook for 2022: Key Priorities for Lasting Agility*, Forbes: *Business Capital Spending In The 2022 Economic Forecast*, Resources & Insights, *2022 Business Outlook Trends for Manufacturing*



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- **Rising raw material costs (cont.)**
 - Another study by *EPS News* suggests that raw material prices will increase 8.2% in the first half of 2022, and that 64% of manufacturers have passed on price increases to their customers.
- **Labor market tightens ... and shrinks**
 - Driven by the effects of the pandemic, the "great resignation," and wage inflation, many manufacturers are facing significant labor shortages. As they look to increase automation and digital transformation, Capex spending in IT is soaring.
 - According to Deloitte, US manufacturers lag their counterparts in countries like Korea, Singapore and Germany in adding advanced manufacturing capabilities including industrial robots. 50% of the executives they surveyed expect to increase operational efficiency through investments in robots and cobots (collaborative robots) in 2022.
 - Manufacturers are facing a critical skills gap which, by 2030, could lead to 2.1 million unfilled manufacturing jobs and a trillion-dollar negative impact on the economy. Attracting new, and especially younger, talent will be critical.
- **ESG is front and center**
 - A study by Deloitte found that 95% of manufacturing executives plan to invest more in ESG initiatives in 2022 than they did in 2021.
 - Hydrogen technologies are of keen interest to many CEOs which may create an attractive landscape for acquisitions. Focus is on emerging technologies that enable the production of "green hydrogen" using renewable energy. Though currently accounting for just 0.1% of the global hydrogen production, its potential for the oil and gas, utilities, metals, transportation, chemicals and agribusiness sectors is profound.

SOURCES: EPS News, *Manufacturers' Capex & Revenue to Expand in 2022*, Manufacturing Global, *Critical manufacturing industry trends to expect in 2022*, Deloitte, *2022 US Manufacturing Outlook*, Mendix.com, *Manufacturing Outlook for 2022: Key Priorities for Lasting Agility*, World Economic Forum, *4 technologies that are accelerating the green hydrogen revolution*.



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- **ESG is front and center (cont.)**
 - More companies hired their first CSO (Chief Sustainability officer) in 2020 than the previous three years combined. The field has grown by more than 228%, from just 29 CSOs in 2011 to 95 in 2021.
 - 68% of CFOs surveyed say that finance takes ultimate responsibility for ESG performance within their enterprise.
 - CEOs are under pressure from stakeholders, especially investors, to increase the transparency of their ESG efforts. But 43% of CEOs admit to struggling to articulate a compelling ESG story.
- **Industry 4.0: from visionary to table stakes**
 - Capabilities around Industry 4.0 – defined as "the transformation of industry through the intelligent networking of machines and processes with the help of information and communication technology (ICT)," and which is used interchangeably with the "fourth industrial revolution" – are impacting virtually every aspect of manufacturing.
 - IIoT – industrial internet of things – was present in only 10% of factories in 2020, according to Gartner. But by 2025, they believe that number will be closer to 50%. The technology holds the promise of interconnecting operations and machines.
 - Additive manufacturing (3D printing) technologies promise to transform manufacturing by providing greater freedom of design, improved plant productivity, sustainable processes and a faster time to market. Industries leading the way, according to Wolters Kluwer, are aerospace and defense, with automotive not far behind.
 - AI – Manufacturers are adopting supply chain solutions which can predict demand and provide supply data in real-time – enabling them to identify vulnerabilities in the supply chain and develop risk management strategies around them.

SOURCES: The Weinreb Group, Accenture, KPMG, Global Manufacturing Prospects 2022, WipFli, Our 2022 outlook for the manufacturing industry, i-Scoop, Manufacturing Net, *Manufacturing Business Trends to Include in 2022*, Wolters Kluwer, *7 manufacturing trends for 2022*



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- **Industry 4.0: from visionary to table stakes (cont.)**
 - 5G deployment may expand in 2022 with advances in technology and use cases, including private 5G networks to enable automation and intelligence on the factory floor, communication with automated guided vehicles and robots, and quality monitoring.
 - Digital transformation/Industry 4.0 is seen as essential to accelerate innovation cycles and better manage disruption, by improving collaboration in what are now siloed operations in which engineering, production, business operations and suppliers are not in alignment.
- **2022 Manufacturing category and Capex outlook**
 - According to an ISM survey, revenues are projected to rise in 15 of 18 manufacturing industries in 2022, with a 7.7% increase in Capex spending (compared to 12.1% in 2021). Sector revenue is expected to increase by 6.5% in 2022 (compared to a 14.1% in 2022).
 - "In reshaping our world toward a new normal, industry should leverage digital transformation at an accelerated pace" reports the World Economic Forum. "To capitalize on the convergence of Industry 4.0 and ESG goals, industry leaders must enable operational efficiency, leverage renewable energy, practice life cycle thinking, and promote supply chain data transparency."
 - Globally, corporate capital expenditures will jump by 13% this year, according to *S&P Global Ratings*, especially in semiconductors, retail, software and transportation. The report cites relative under-investment in manufacturing over the last number of years. Capex concerns include lost momentum as consumer demand cools, or a goods shortage turning into a supply glut. "For now, companies are betting they have more to lose from not upgrading."

SOURCES: Deloitte: *2022 US Manufacturing Outlook*, Strategic Finance, *What's keeping CFOs up at night in 2022?*, The Industrial Transformation Network, *4 Trends That Will Dominate Manufacturing in 2022*, ISM: *Manufacturers expect revenues to rise in 2022, from 2021*, The Economic Times, *Global Capex booms as companies prepare for post-pandemic era*



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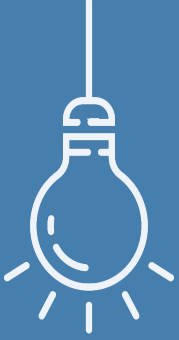
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- **2022 Manufacturing category and Capex outlook (cont.)**
 - According to *EPS News*, factories are now operating at 88.7 percent of their normal capacity, up 0.4 percentage points from May 2021 – an increase achieved by adding personnel, hours, new plants/equipment, and fewer shutdowns.
 - 78% of manufacturers had a more positive outlook for 2022 than they did in 2021 according to a *Reports & Insights* study. When respondents were asked in what areas they plan to increase their capital spend, almost half indicated acquiring new locations or facilities. Research and development and training employees tied for second at 30.4% each.
 - PWC: “We are seeing a record level of transactions in the industrial manufacturing and automotive sectors powered by an abundance of capital and a growing number of private equity deals. We expect M&A in 2022 to remain strong with high multiples.”

SOURCES: EPS News, *Manufacturers' Capex & Revenue to Expand in 2022*, PWC Global, *Global M&A Trends in Industrial Manufacturing & Automotive Sectors: 2022 Outlook*



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CAPEX Considerations

- **Role of FP&A** is increasingly being tasked with finding efficiencies and identifying opportunities to improve revenues and profitability across the entire company.
- **Capex re-evaluation:** Having faced cash flow pressures in 2021, organizations were compelled to revisit and reevaluate their Capex projects. Now, again in 2022, as myriad forces impact supply and demand, companies once again have to determine where to make strategic investments (in production capacity, for example), which maintenance/sustaining projects can't wait, and so forth. Making informed choices across a portfolio of projects is when a Capex management system such as Finario truly shines, helping companies make faster, better decisions based on up-to-the-minute data, ROI analyses, and more
- **Agile decision making:** At a time when tariffs, regulations, politics, new technologies, and variability in demand present formidable challenges for manufacturing executives, the ability to pivot quickly, react opportunistically, and make capital decisions that are well-considered, strategic, and based on a holistic view of capital projects in progress or in consideration, can have a material impact in the millions
- **Personal hygiene/safety:** Manufacturers are faced with new challenges to accommodate and innovate in terms of their perceived and real safety risks. How much of this will be the "new normal" vs. a temporary necessity challenges Capex choices
- **Modern Manufacturing:** Ongoing opportunities to improve efficiency and expand market share continue to push modern manufacturing technologies that automate processes, meet sustainability goals and mandates, and connect operations to finance; these strategic, growth-minded projects need to have the visibility and vetting rigor to ensure appropriate consideration
- **Rolling Forecasts:** As supply chain issues persist, the ability to budget and forecast accurately and continuously increases; this is extremely difficult to do utilizing spreadsheets and other manual tools -- creating yet another business case for a purpose-built capital planning software solution

FINARIO // The SaaS Solution for Capex

Finario provides a connected capital planning solution to leading global enterprises. Our cloud-based platform creates a single source of truth for Capex, integrating and aggregating detailed project cost data from all of their related systems to support streamlined processes that foster collaboration between finance and operations. Purpose-built for the job with sophisticated financial intelligence on a robust project foundation, Finario provides the real-time analytical support decision makers need to make the most of their capital investment and enhance their organization's long-term growth and profitability.