Deloitte
Belgian CFO Survey
Corporates are defensive

Benchmarking corporate financial attitudes

CFO Services
Second quarter edition 2012 - July 2012

Content

"Little of the optimism the survey reported last quarter remains. Worries about recession and a breakup of the euro have knocked business confidence again"

Key points from the 2012 Q2 survey

- The general level of economic and financial uncertainty has gone up again in the second quarter. The increase in optimism in the first quarter has not sustained: CFOs are significantly less optimistic today about the financial prospects of their own organisation than they were three months ago.
- CFOs do not expect the economy to recover soon: only 20% of CFOs expect demand for their products and services to take up before the end of the year – down from 60% three months ago. 25% do not expect improvement before 2014.
- Halfway through the year 60% of surveyed CFOs report financials are lagging behind budget, up from already 40% at the end of the first quarter – and significantly more than in the previous years.
- On balance, bank borrowing is perceived as neither attractive nor unattractive. Although overall CFOs are not overly concerned with external financing, 40% currently perceive credit as costly and hard to get. Going forward, two thirds of CFOs anticipate harder pricing and/or lending terms for bank borrowing.
- CFOs remain focused on defensive strategies such as boosting cash flow and cutting costs. Capital expenditure and mergers and acquisitions are not top of the list.
- Although 40% believe one or more countries might leave the Eurozone in the next 12 months, only a quarter reports that their company is changing its plans to deal with the risk of the euro stress. One third of the CFOs, mainly representing large organisations, who foresee at least some effect on their business from a breakup of the euro, have at least made some preparations in the event it would happen. However only few are already well prepared.

The macroeconomic backdrop to the Deloitte CFO Survey 2012 Q2

"The euro area crisis intensified, driven by the political instability in Greece and market concerns over Italian and Spanish solvency. Although the European Union agreed to bail out Spanish banks, level of financial and sovereign stress remained elevated. The OECD warned that the euro debt crisis has become the most important source of risk to the global economy. Outside the euro area, a series of weak economic data from the US and the emerging market economies compounded concerns over global growth prospects."

Ian Stuart, Chief Economist Deloitte UK

Volatile. If there is one word that best describes the current financial and economic environment, this might be it. The general level of economic and financial uncertainty has further increased in the second quarter. Little of the optimism the survey reported last quarter remains. Worries about recession and a breakup of the euro have knocked business confidence again. But CFO pessimism is not just driven by the mood of the day. Many organisations report disappointing financials halfway through the year. Old certainties are being questioned, and decisions made several months ago are now being reconsidered. Defensive strategies are on top of the agenda.

Mood swings

Things were looking up again in the first quarter of the year. Many CFOs seemed to have shaken much of the gloom displayed at the end of last year. Well almost. The increase in CFO optimism in the first quarter has not sustained. CFOs are again significantly less optimistic today about the financial prospects of their own than they were three months ago.

The underlying causes of Europe's debt crisis – uncompetitive economies and indebted governments – remain, and will not be solved in the short run. The future of the Eurozone remains at risk. Consumer demand is far from reassured and projections for growth for many of the European countries - but also the US - are challenged. High growth economies such as China are slowing down as well.

CFOs expectations on the timing of the recovery of the Belgian economy have been pushed back by at least half a year. And unlike the previous quarters, CFOs are no longer more optimistic about the prospects for their own company than for the economy as a whole. Today only 20% of CFOs expect demand for their company's products and services to take up again before the end of this year – down from 60% three months ago. 25% anticipate a very slow recovery and see no significant improvement before 2014.
Not a surprise that the economic recovery is the CFOs main concern, next to securing their competitive position in the market.

Poor performance and outlook

Close to 60% of CFOs now report that the actual performance of their company is lagging behind the budget, up from already 40% at the end of the first quarter. To put this into a longer term perspective: in 2010 only 20% of CFOs reported worse than expected performance in the second quarter, in 2011 it was 30%. Today, this percentage has doubled compared to 2011. On average, CFOs expect only marginal top line growth and further decreasing operating margins going forward. Taking into account that CFOs were already very pessimistic in the fourth quarter of 2011 - when many prepared their 2012 budgets – these second quarter results illustrate the significant challenges that many organisations face.

No appetite for risk

CFOs do not think the time is right to take on additional risk on the balance sheet. Risk appetite has plummeted back to the low levels we reported coming out of the recession in the first quarter of 2009.

Fewer CFOs plan to reinvest surplus cash back into the business. With financial and economic uncertainty significantly above normal levels, CFOs remain focused on defensive balance sheet strategies such as boosting cash flow and cutting costs. CFOs see hiring and discretionary spending declining over the next year.

Capital expenditure and mergers and acquisitions are hence not top of the list. In search of growth and to avoid stagnation, expansion into new markets or products remains important for more than one third of the respondents.

Financing

The attractiveness of the major forms of financing – equity, bank borrowing and corporate debt - has lowered somewhat compared to the first quarter.

On balance, bank borrowing is perceived as neither attractive nor unattractive. Although overall CFOs are not overly concerned with external financing, 40% currently perceive credit as costly and hard to get. Macroeconomic uncertainty and the outlook for demand appear to have greater influences on capital spending than the availability of finance.

Going forward two thirds of CFOs anticipate harder pricing and/or lending terms for bank

Euro worries

The Eurocrisis is not over. Over 40% of the survey respondents assign a high rating to the likelihood of one or more member states leaving the Eurozone in 2012, and a quarter reports that their company is changing its plans to deal with the risk of the euro stress.

Although one out of three CFOs expect a significant effect on their business in the event of one or more member states leaving the euro, only 6% of the respondents expecting at least some effect from this event, consider themselves well prepared for this event. 27% of those respondents, mainly representing large organisations, have made some preparations.

Wage indexation

CFOs endorse most of the recommendations the European Commission has made to the Belgian government at the end of the first quarter. First priority for the CFOs is the reform of the system of wage bargaining and wage indexation. The political reactions on the recent Central Bank report on the wage indexation system predict a difficult debate.

What CFOs can do

Companies are faced with specific challenges in today's uncertain economic environment. Economic uncertainty is the biggest constraint on corporate expansion. The challenge for companies is to find sources of growth in a volatile macroenvironment.

CFOs need to develop playbooks to ensure the availability of cash and value, navigate the current downturn, renew growth under varied economic-recovery scenarios, and manage risk. Here is how you could get started.

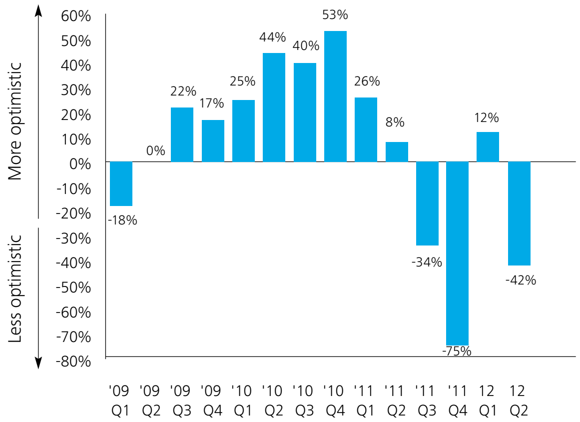
A critical priority for most CFOs is to assure sufficient cash for their company to operate without interruption. In the current environment, CFOs must also secure financing in the coming three to five years and identify opportunities to improve access, cost and flexibility of financing. Forecasting near-term revenues and providing earnings guidance is another key challenge for CFOs. Strong revenue-forecasting tools are essential to successfully managing finances and cash flow.

Thierry Van Schoubroeck,
Partner

Confidence drops

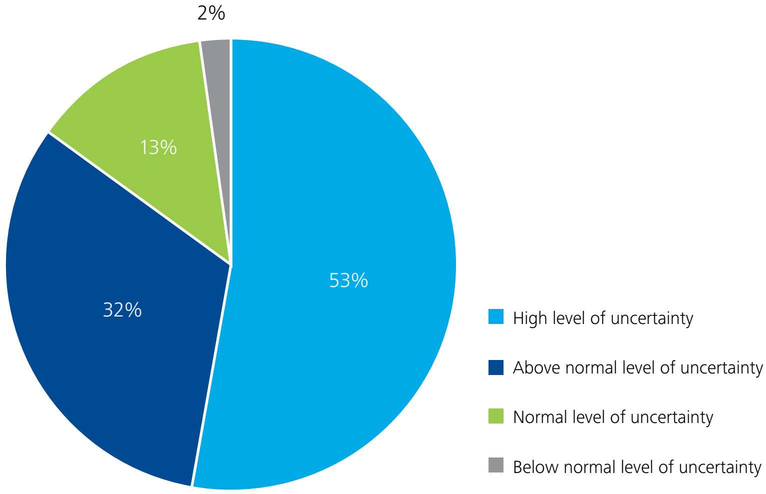
Worries about recession and a breakup of the euro have knocked business confidence again. The more optimistic mood witnessed in the first quarter of 2012 has not sustained: CFO optimism has seen the sharpest fall since the CFO survey started in Q1 2009.

Net % of CFOs who are more/less optimistic about financial prospects for their company



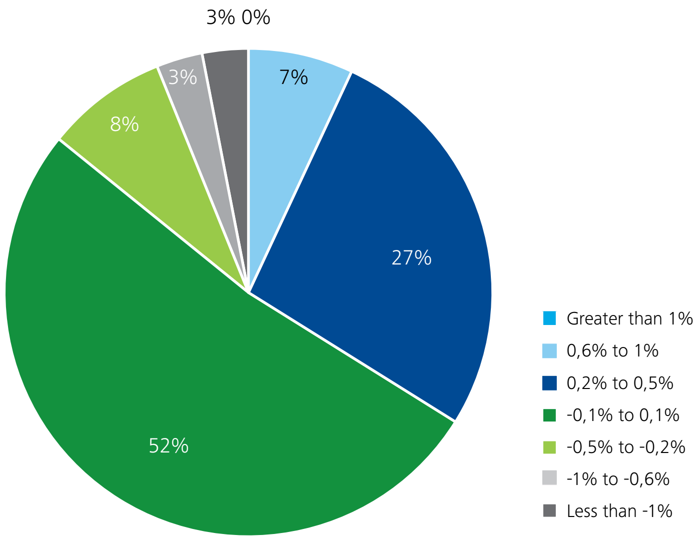
The volatile pattern in CFO optimism coincides with the general level of external financial and economic uncertainty amongst CFOs. 85% of Belgian CFOs believe their businesses face a high or above normal level of uncertainty.

CFOs' rating on the general level of external financial and economic uncertainty facing their business



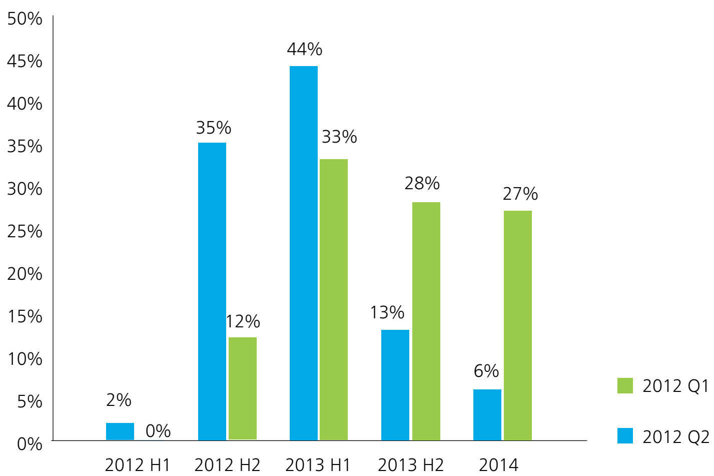
On average CFOs expect very little growth for the Belgian economy in 2012. Expectations are in line with earlier communicated forecasts made by Belgian and European authorities. Half of the survey respondents expect flat growth, between -0.1% and 0.1%.

CFOs' expectations for the Belgian economic growth in 2012



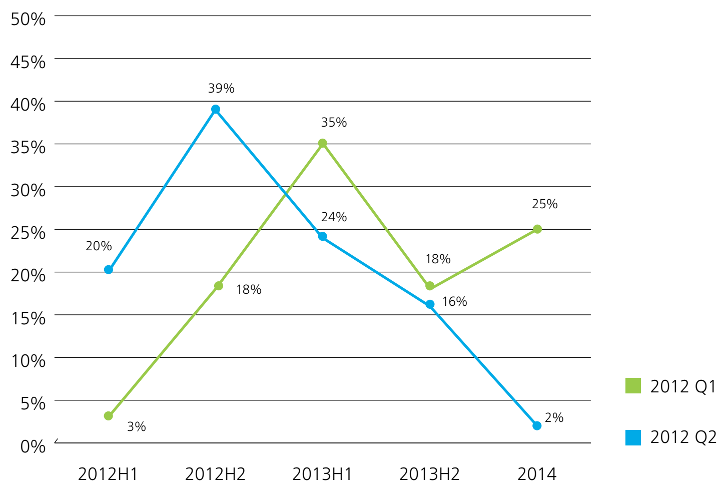
The expected timing of recovery of the Belgian economic growth has significantly shifted back compared to the previous quarter. CFOs expect the recovery to be slow: only 45% believe the Belgian economy will take up again in the next 12 months, down from 80% three months ago.

CFOs' expectations about timing of recovery of the Belgian economic growth



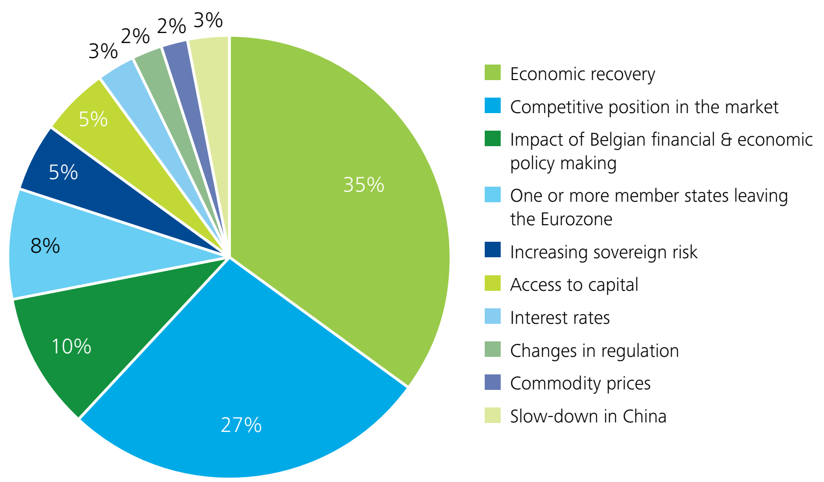
The expected timing for the acceleration of the growth in demand for their own organisations' products and services has shifted back as well. Unlike in the previous quarter, CFOs are no longer more optimistic about the prospects for their own company than they are for the economy as a whole.

Expected timing for acceleration of growth in demand for products and services of CFOs businesses



It is not a surprise that the economic recovery is the CFOs main concern, next to securing their competitive position in the market. The challenge for companies is to find sources of growth in a volatile macroenvironment. Concerns about the impact of the Belgian government's financial and economic policy making have eased somewhat.

CFOs' perception on the greatest concern for their business in 2012

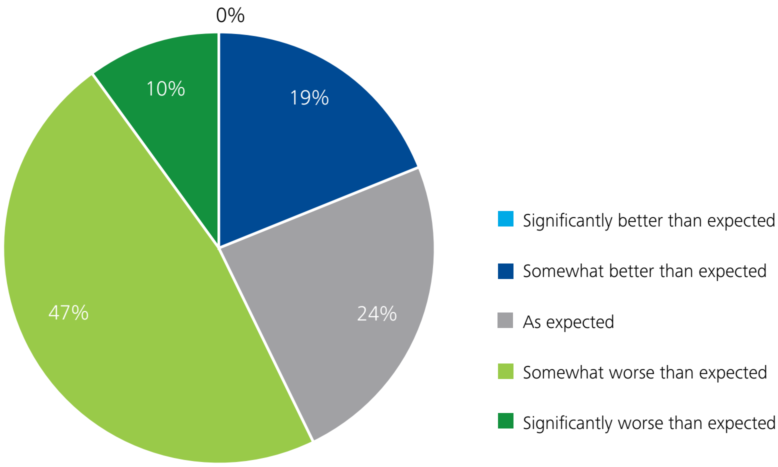


"After six months, actuals are disappointing for many organisations: almost 60% of the CFOs report that their organisation is already performing worse compared to budget"

Disappointing financials

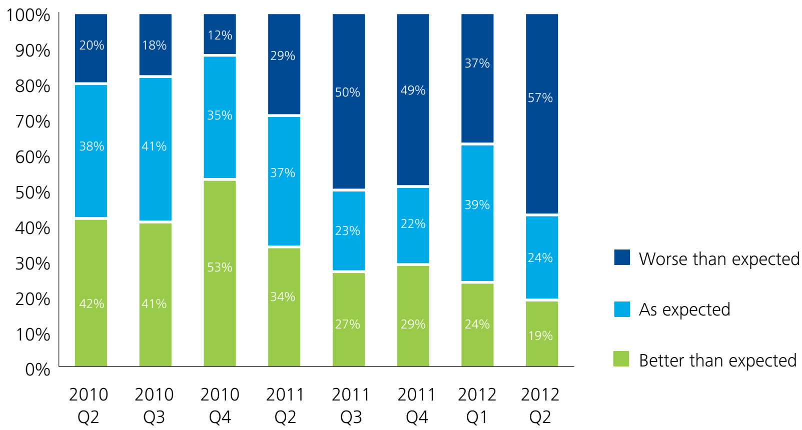
Halfway through the year almost 60% of the CFOs report that financial performance is not in line with budget.

Comparison of the surveyed organisations' actual performance versus budget



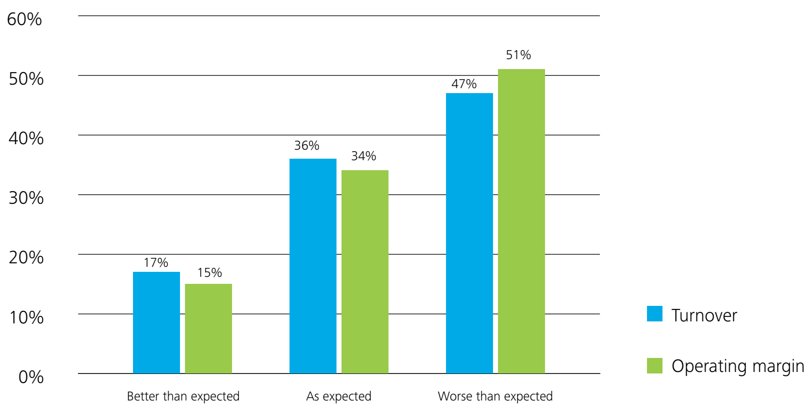
Compared to the first quarter, the percentage of CFOs reporting worse than expected performance, has increased significantly. In the first quarter of 2010, only 20% of CFOs reported worse than expected performance. In the second quarter of 2011 it was 30%. Today, this percentage has doubled compared to 2011 . These figures give reason to worry, also because CFOs were very pessimistic at the end of 2011 – when many of them were preparing the 2012 budget.

Comparison of the surveyed organisations' actuals performance versus budget



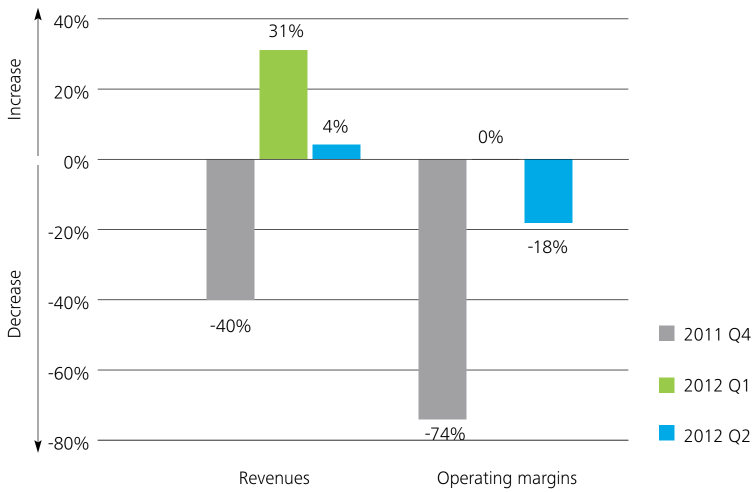
A similar trend can be observed when looking at the actual turnover and operating margin versus the budget: both metrics are worse than expected for about half of the organisations.

Comparison of the surveyed organisations' actual turnover & operating margin versus budget



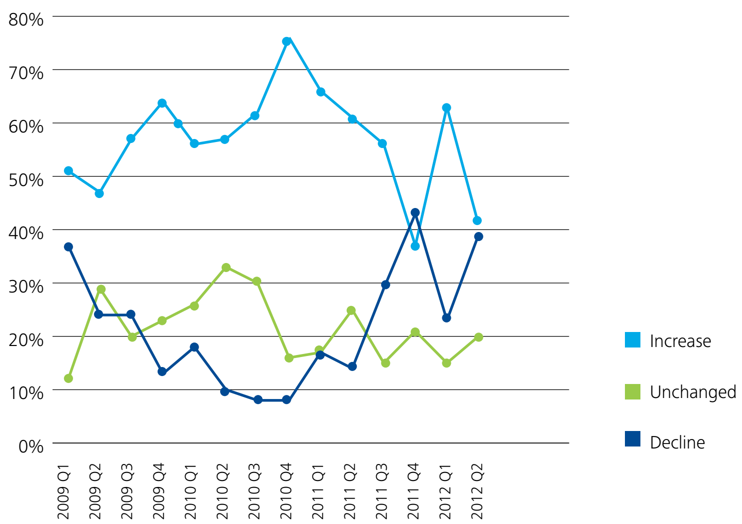
On balance, CFOs see operating margins further shrinking over the next year. The general expectation is that turnover will remain flat.

Net % of CFOs expecting an increase/decrease of the following key metrics for their companies in 2012



CFOs have again become significantly more negative on the outlook for cash flow. While at the end of the first quarter over 60% predicted the operating cash flow of their company to go up over the next twelve months, this percentage has dropped again to 40%, back at the low level of the end of 2011.

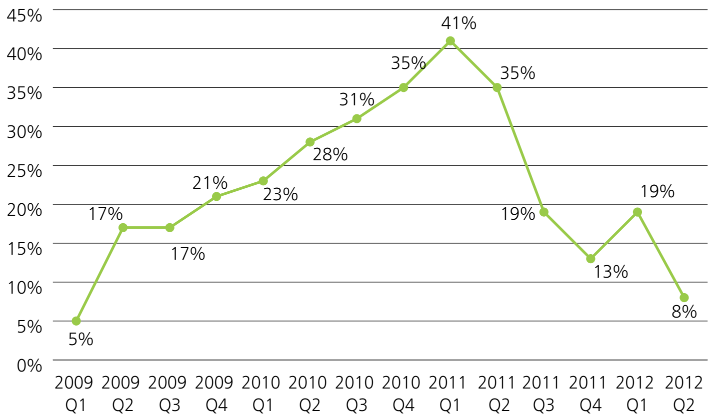
CFOs' expectations for the free cash flow evolution for their company over the next 12 months



Corporates defensive

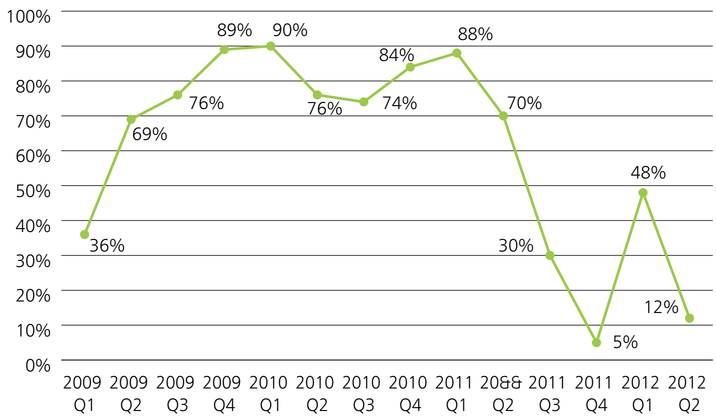
Risk appetite is back at the very low level of early 2009. CFOs are not planning major investments in the near future.

% of CFOs who think now is a good time to be taking greater risk onto their balance sheet



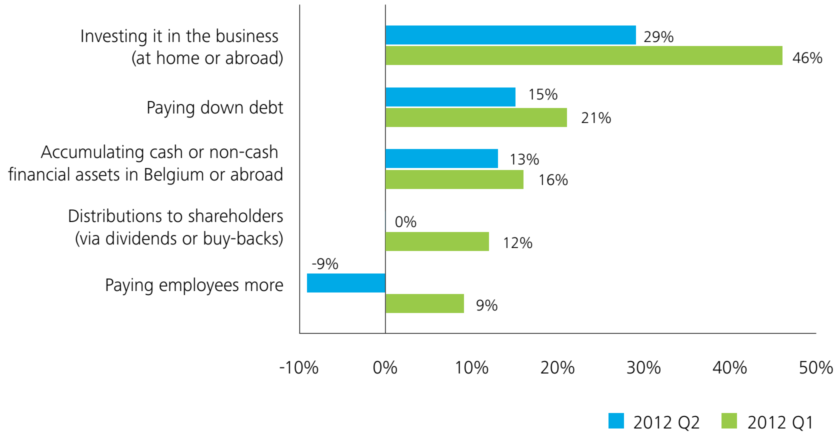
Expectations for mergers and acquisitions remain low and, are very much correlated to the risk appetite.

Net % of CFOs who expect M&A activity to increase over the next 12 months



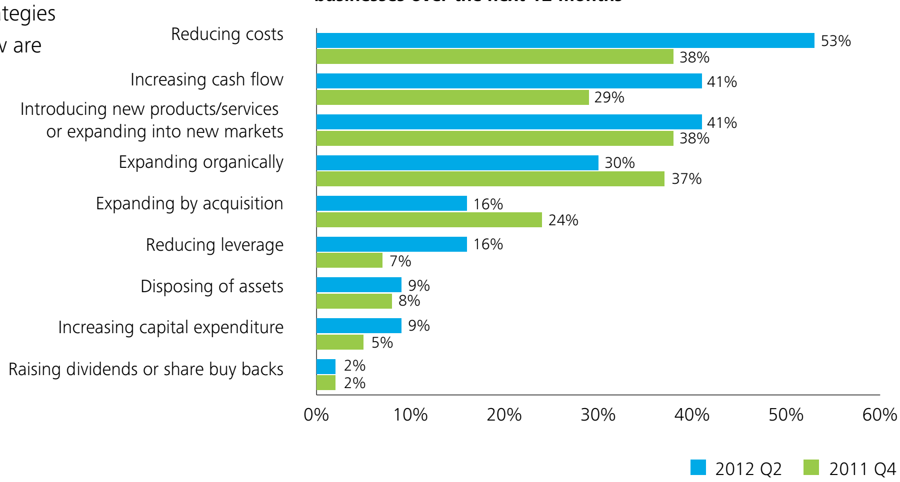
Appetite to re-invest the surplus cash in the business has decreased compared to previous quarter.

Use of "surplus" cash by a net % of CFOs



Declining optimism and risk appetite have manifested themselves in a shift towards more defensive strategies by CFOs. Reducing costs and increasing cash flow are the top priorities for Belgian CFOs.
Expansion is less popular than 6 months ago.

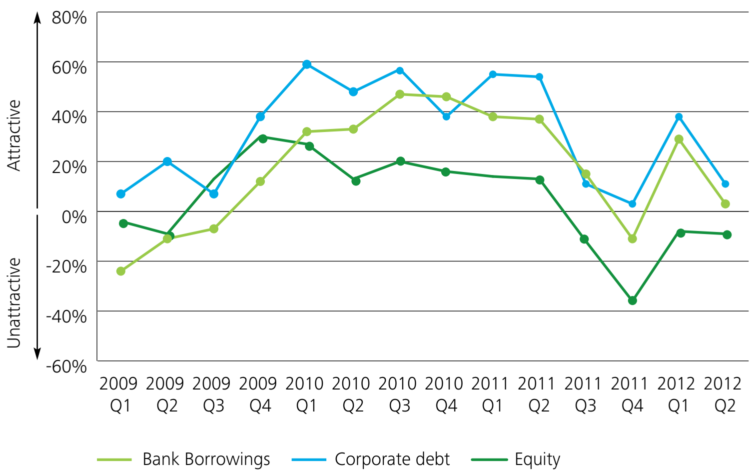
Business strategies likely to be a priority for the CFOs businesses over the next 12 months



Credit conditions weaken

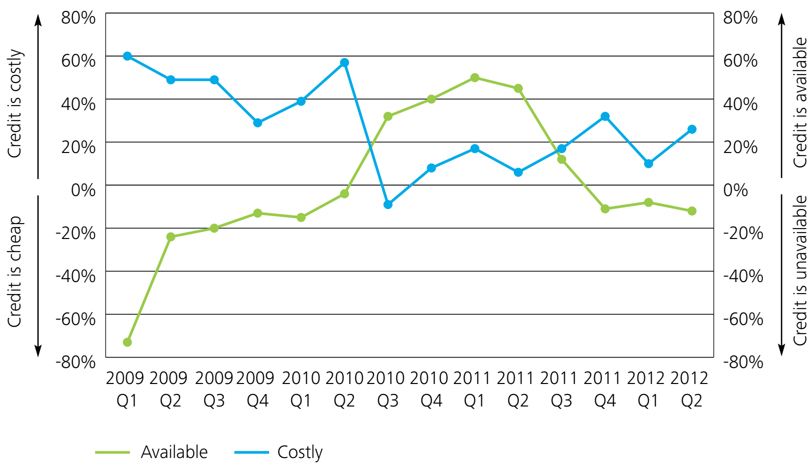
Bank borrowings and corporate debt have lost attractiveness compared to the previous quarter, and are again at the level of end of last year. On balance, all forms of financing are now perceived as neither attractive nor unattractive.

Net % of CFOs reporting the following sources of funding as attractive/unattractive



Compared to previous quarter, credit is perceived as more costly and slightly less available. Despite the deterioration in the cost of credit, credit conditions on average do not seem to be especially stringent.

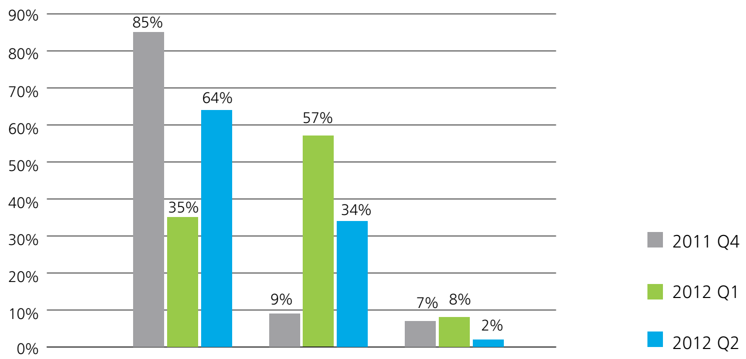
Net % of CFOs reporting credit is costly and net % reporting credit is available



"Going forward, two thirds of CFOs anticipate harder terms for bank borrowing"

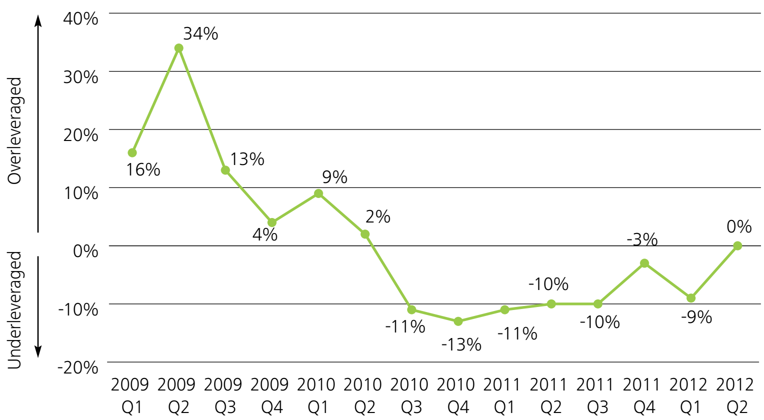
Going forward two thirds of CFOs anticipate harder pricing and/or lending terms for bank borrowing. Though the expectations on the evolution of the price and lending terms vary from quarter to quarter, the dominant view suggests continued financial stress.

CFOs' expectations about evolutions of price terms and lending terms in the next 6 months



On average balance sheets for Belgian corporates are appropriately leveraged.

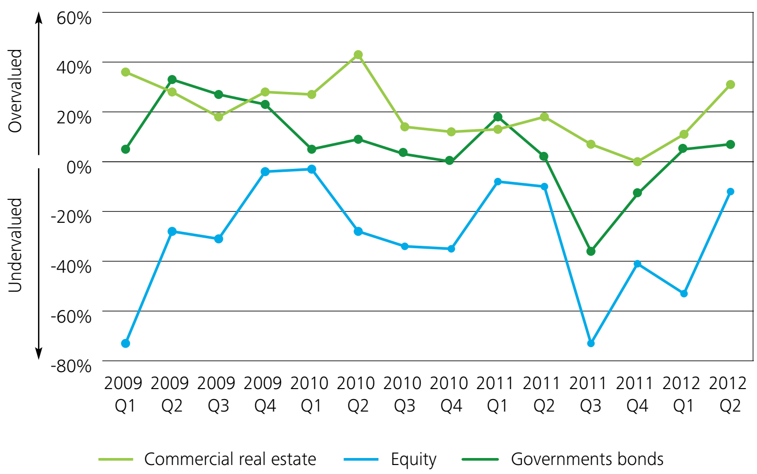
Net % of CFOs who think Belgian corporate balance sheets are overleveraged/underleveraged



Equity recovers

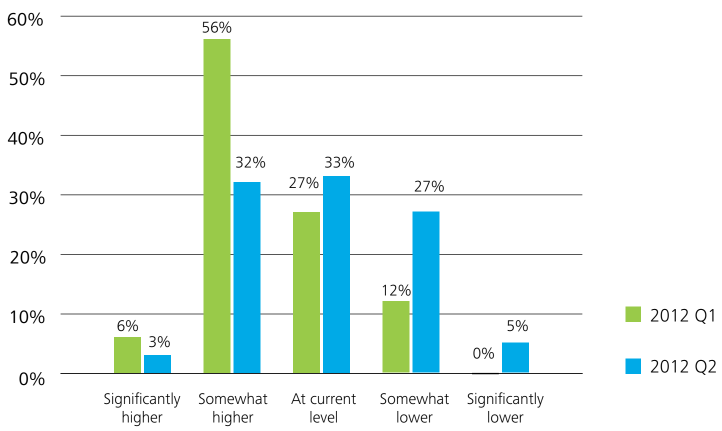
Compared to the previous quarter the perception of the valuation of equity has improved significantly: on average equity is now perceived as only slightly undervalued. As during the previous quarter, government bonds are perceived adequately priced; commercial real estate is perceived as more overvalued.

Net % of CFOs who think the following assets are overvalued



Although the perception of the valuation of equity has improved significantly compared to last quarter, the expectations for the Bel 20 in a year's time have lowered: the percentage of respondents expecting an increase has decreased from over 60% to about 35%.

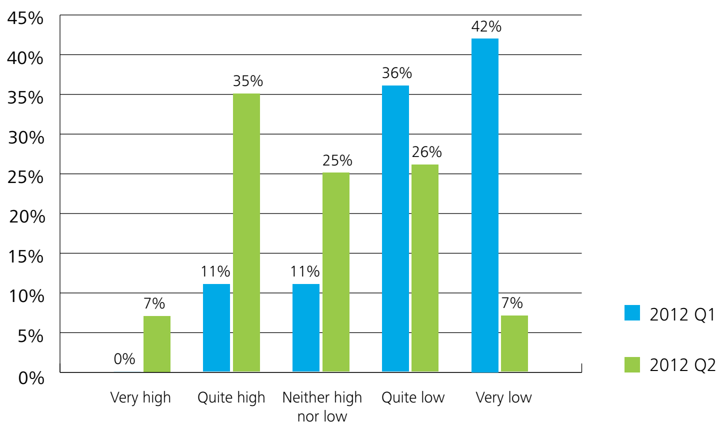
CFOs' expectations for the Bel 20 in a year's time



Eurocrisis deepens

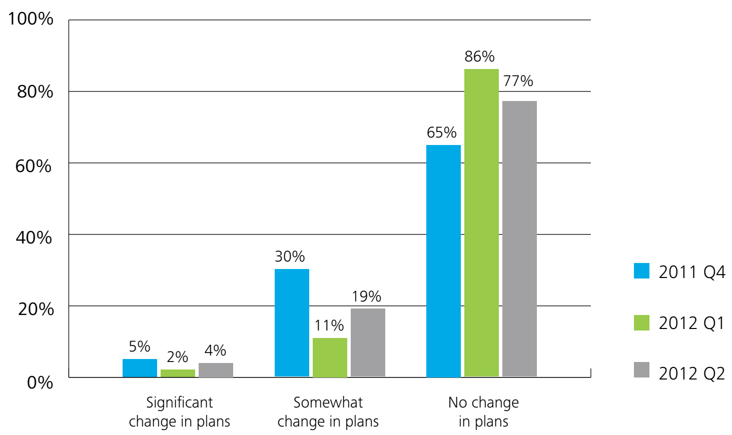
The Eurocrisis is not over. Over 40% of the survey respondents assign a high rating to the likelihood of one or more member states leaving the Eurozone in 2012, compared to 10% last quarter.

CFOs' rating on the likelihood of one or more member states leaving the Eurozone in the course of 2012



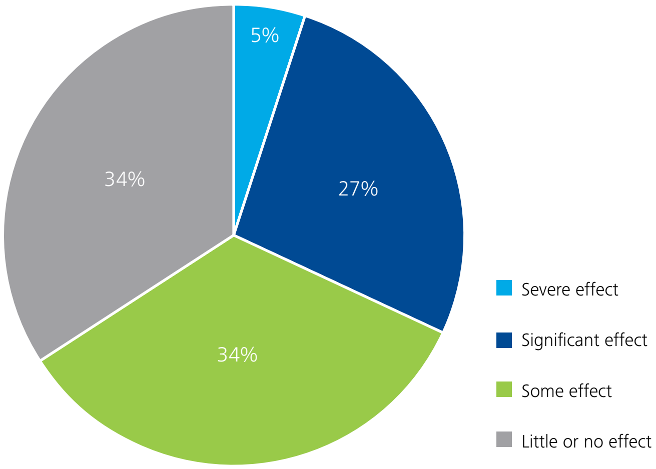
Nevertheless, only one in four CFOs report that their company is at present changing plans to deal with the risk of the euro stress; up from about 13% reported during the previous quarter but still lower than 6 months ago.

Extent to which companies are changing their plans to deal with the risk of the euro stress

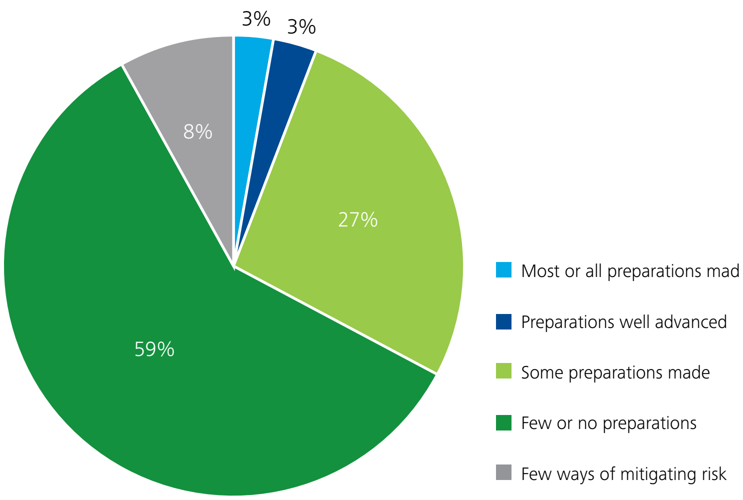


Although one out of three CFOs expect a significant effect on their business in the event of one or more member states leaving the euro, only 6% of the respondents expecting at least some effect from this event, consider themselves well prepared. 27% of those respondents, mainly representing large organisations, have made some preparations.

CFOs’ expectations on the effect on their company's business in the event of one or more member states' departure from the Euro



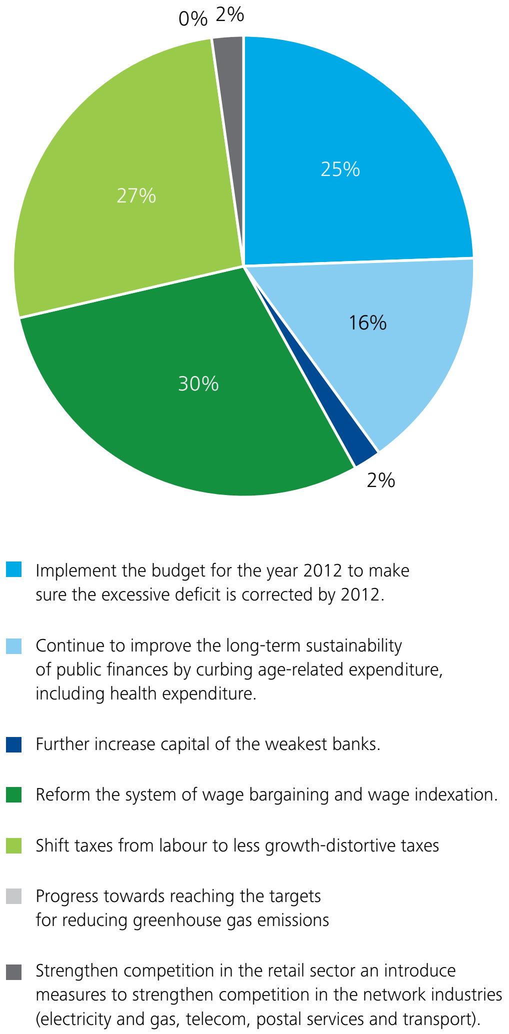
***CFOs’ rating on their business preparedness for a full or partial breakup of the Euro**



* Of those CFOs who foresee 'some', a 'significant' or a 'severe' effect on their business from a breakup of the euro (see previous chart)

At the end of May, the European Commission formulated a new set of recommendations for Belgium. On average, CFOs rating on the importance of these seems to be spread rather equally between implementation of the budget, reforming the system of wage indexation, shifting of taxes and improving long-term sustainability of public finances. Although further increasing capital of the weakest banks was suggested to ensure granting of credits and liquidity, this recommendation is not considered a priority for CFOs.

CFOs rating on the importance of the recommendations expressed by European Commission



Implications for the CFO

Companies are currently faced with specific challenges, questions and concerns that are caused by today's uncertain economic environment.

A critical priority for most CFOs is to assure sufficient cash for their company to operate without interruption. CFOs can focus on improving disciplines around cash management, analyse and understand drivers of cash flow. CFOs can focus on the completeness of the current top line. It is easy money, waiting to be processed, invoiced and collected. CFOs must secure financing – not only short term but for the coming three to five years – and identify opportunities to improve access, cost and flexibility of (debt) financing.

But CFOs can also create value through identifying enterprise-wide cost reduction opportunities, and through taking advantage of tax planning opportunities that help business weather difficult times.

Most recessions since World War II have lasted less than a year, but the current slowdown might continue through 2013 or longer. What can CFOs do in this environment? The first thing is to track indicators that provide a likely trajectory for recovery. The challenge for CFOs will be to read the signals and discern the shape and structure of the recovery. We hope the CFO survey can contribute to this.

CFOs need to develop playbooks to navigate the current downturn, renew growth under varied economic-recovery scenarios, and manage risk. Forecasting near-term revenues and providing earnings guidance is a key challenge for CFOs. Strong revenue-forecasting tools are essential to successfully managing finances and cash flow.

The CFO can also act as the ‘voice of reason’ of the company. In good times this means keeping everyone’s feet on the ground, and safeguarding the organisation from overly ambitious or risky ventures. But in difficult times, the CFO is often well positioned to see investment opportunities, when the rest of the organisation is still focusing on day-to-day survival.

The Deloitte Belgian CFO Survey is produced by Thierry Van Schoubroeck, Partner and Ann Moerman, Senior Consultant.

A note on methodology

Not all survey questions are reported in each quarterly survey. In response to the current financial economic situation survey questions will be selected. In case you participated to the survey and would like to receive information about non-reported questions do not hesitate to contact us.

Some of the charts in the Deloitte CFO survey show the result in the form of a net % balance. This is the percentage of respondents reporting, for instance, that bank credit is attractive minus the percentage saying bank credit is unattractive. This is a standard way of presenting survey data.

The 2012 second quarter survey took place between 31 May and 27 June, 2012. A total of 60 CFOs completed our survey. The participating CFOs are active in a variety of industries. 23% of the participating companies have a turnover of over 1 billion, 53% of between 100 million and 1 billion, and 25% of less than 100 million.

We would like to thank all participating CFOs for their efforts in completing our survey. We hope the report makes an interesting read, clearly highlighting the challenges facing CFOs, and providing an important benchmark to understand how your organisation rates among peers.

Delivering the voice of the CFO community

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