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CFO Survey

Bosnia and Herzegovina | January 2014

After the fall in GDP in 2012, Bosnia and Herzegovina reported flat growth of 0.5% in 2013. In 2014, GDP is expected to grow by 1.5%.

Despite this challenging time for businesses in Bosnia and Herzegovina, corporate expectations for 2014 are optimistic

It is our pleasure to present the results of the first edition of the Deloitte Central Europe CFO Survey to be conducted in Bosnia and Herzegovina (BiH). This is part of an established regional survey that Deloitte has regularly conducted and published for several years in Central Europe. This edition addresses the views of and issues affecting BiH Chief Financial Officers (CFOs), comparing their sentiments with those of their peers from other economies in the region, including Albania and Kosovo,Bulgaria, Croatia, the Czech Republic, Hungary, Latvia, Lithuania, Poland, Romania, Serbia, Slovakia, and Slovenia.

The past 12 months were characterised by marginal GDP growth which was due to stronger exports and industrial production. These factors, alongside the construction of the motorway VC corridor and investments in thermo and wind-power plants, may stimulate and support slightly more growth in 2014. But there are no signs of a sustainable and strong economic recovery, hampered by delays in EU accession, limited progress on reform implementation, strict IMF conditions restricting public spending, falling real wages and rising unemployment.

The results for this year show that many CFOs are more optimistic about the prospects for their own firms than they are for those of the economy as a whole. This is a challenging time for businesses and economy in Bosnia and Herzegovina. The tough economic environment is making revenue growth and cost-cutting key priorities for companies to deal with. However, in 2013 the majority of interviewed CFOs reported single-digit or no growth in revenues, while only 15% reported a drop in the sales figures. Corporate expectations for 2014 are better, and no declines in sales or profits are expected.

We hope that you find this publication interesting and useful; Iwe would also like to invite you to take part in the next survey to be held in late 2014.

Miloš Macura
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Key trends and findings:

- Despite financial and economic uncertainties, a majority of BiH CFOs feel optimistic about their companies' financial prospects
- Cost reduction and growing revenues from existing and new markets are seen as priorities for the year ahead
- BiH CFOs predict that the economy will keep stagnating in the next year (71% predict stagnant growth in GDP)
- A slight increase in unemployment levels is expected in the coming period, while significant talent shortages are anticipated for the finance area, particularly at the middle and top levels.

Economic outlook for 2014

The BiH economy is struggling and is set to grow slowly due to the Europe-wide crisis, which will hinder investment and trade. Growth is slow because of a poor export performance; in addition, we continue to face high unemployment, a lack of confidence and low industrial production. It is very likely that this situation will remain unchanged for the near future. Hence, the BiH economy continues to be fragile, politically paralysed and dependent on foreign transfers.

The Bosnian Convertible Mark is pegged to the Euro, and the money in circulation is matched by foreign exchange reserves.. Even though some experts claim that the currency board is not a favourable option for domestic production, exports and economic growth, it provides stability and forces the governments of the two entities to practice financial prudence (i.e. to finance themselves exclusively through taxation and borrowings).

Inflation stood at 2.1% in 2012, and annual inflation rates averaged 0.5% in 2013. A slight drop in consumer prices in August and September was a result of weak domestic consumption, rising unemployment, declining real wages and low remittance inflows. It is expected that inflation will increase slightly in 2014 as growth picks up, and should average 1.4%.

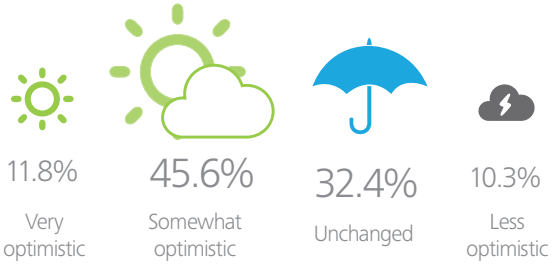
Weak domestic demand in conjunction with economic and political uncertainties will have an important impact on how business develops in the short term. Mixed economic fundamentals will largely prevent a stronger recovery, combined with an on-going brain drain and the reluctance of foreign investors to use the country as a cheap manufacturing base. However, growth of 1.5% is expected in 2014, rising to 2.5% in 2015.

Findings – prospects and predictability

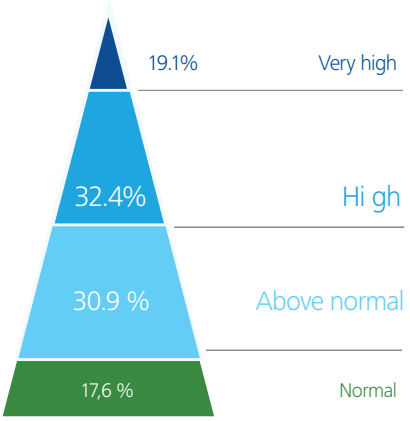
Our survey indicates that 57.4% of CFOs are more optimistic about the financial prospects of their companies compared to the beginning of 2013, while 32% remain unchanged in their views. Only 10.3% see future prospects as less positive. This is a clear indication that a slow recovery is expected, but that a significant proportion of the interviewed CFOs remain concerned about the financial prospects for their companies.

63% of interviewed companies rated the general level of external financial and economic uncertainty facing their businesses as high or above normal. Accordingly, it is understandable that 75% of the interviewed CFOs also believe that this is not a good time to be taking greater risks on to company balance sheets.

Graph 1: Compared with six months ago, how do you feel about the financial prospects for your company?



Graph 2: How would you rate the general level of external financial and economic uncertainty facing your business?



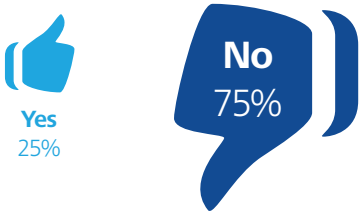
Only 25% of interviewed CFOs believe that this is a good time for new investments and taking more risks on to company balance sheets.

This correlates with the GDP growth expectations of BiH CFOs. Our survey shows that a majority of participants (71%) expect stagnation, while 21% expect moderate growth and 8% expect recession.

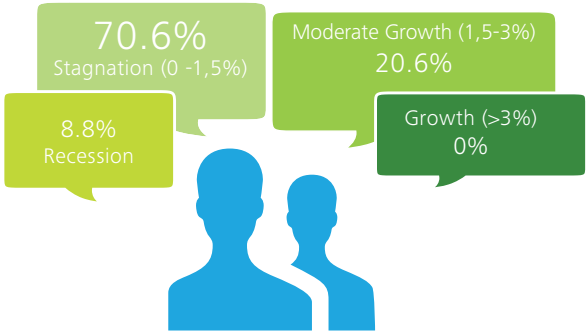
Unemployment is yet another area in which an unfavourable trend is expected. Our winter survey shows that 42% of participants now expect no change. At the same time, it shows that 38% of respondents expect a moderate increase, and 4% a significant increase, in the numbers of unemployed.

Corporate expectations for 2014 are better than last year – a majority of CFOs do not expect either sales or profits to decline.

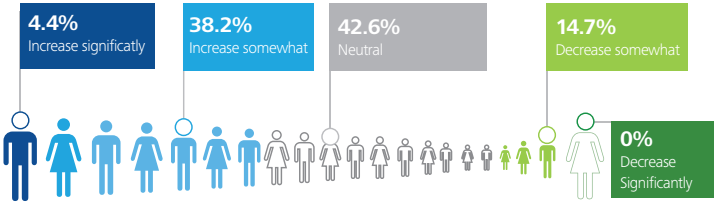
Graph 3: Is this a good time to be taking greater risk onto your company's balance sheets?



Graph 4: CFOs' expectations for the country's economic GDP growth in 2014



Graph 5: Over the next 12 months how do you expect levels of unemployment to change in your country?



The focus for the year ahead

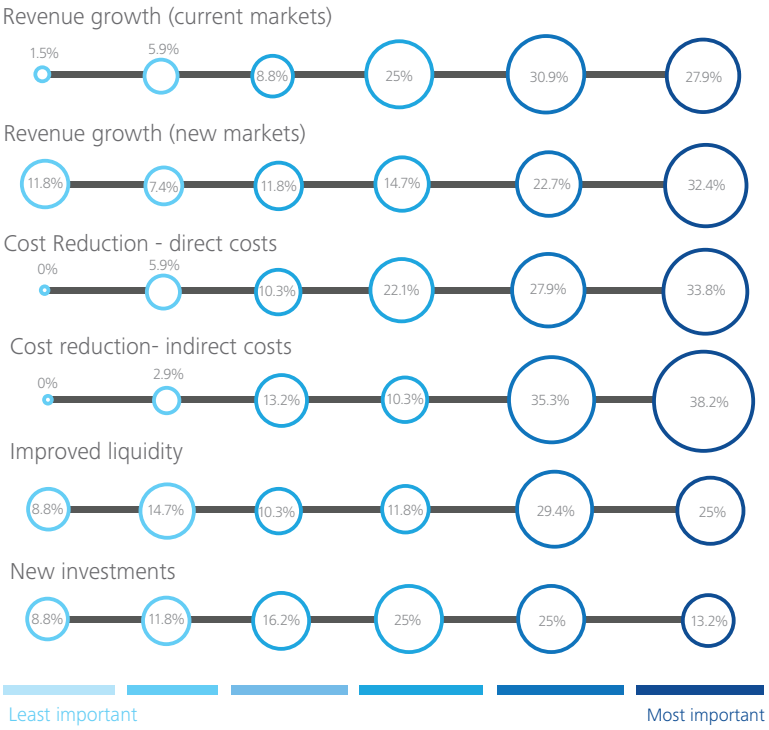
More than half of our respondents said that growing revenues in current and/or new markets was their key priority for the year ahead, while a vast majority will focus on reducing costs. This corresponds to an overall impression among BiH CFOs regarding the future outlook of the economy: they are being 'stretched' between strategies – on the one hand to preserve market share or consolidate internally through the better use of available resources, and on the other to achieve growth.

54% of CFOs stated that improving liquidity is an important or the most important focus for the next 12 months.

Consistent with these findings is the statement that BiH CFOs are not keen on new investments and that over a third of participants do not see new investments as a high priority.

A majority of BiH CFOs have revenue growth, cost reduction and liquidity improvement as their key priorities for the next year.

Graph 6: What is your company's business focus for the next 12 months?



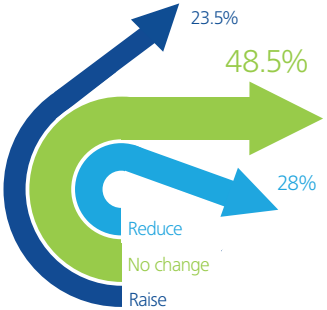
Sources of finance

Almost half (49%) of the CFOs expect no change in their companies' gearing ratios in the year ahead. 28% are aiming to reduce gearing while 23% aim to raise their gearing ratio.

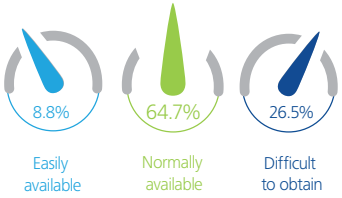
27% of the CFOs we interviewed believe that new credit will be difficult to obtain. On the other hand, the great majority believes that new credit is easily or normally available. This is in line with macroeconomic data that show an increase in domestic savings and deposits.

On the other hand, the growing proportion of non-performing loans is driving banks to impose additional provisions and demand unfavourable financing terms. This is consistent with the expectation that the costs of finance will increase, although it appears that only 6% believe that this increase will be significant.

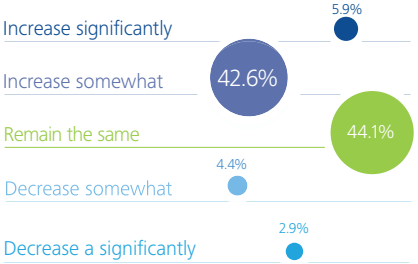
Graph 7: What is your aim for your level of gearing over the next 12 months?



Graph 8: How would you rate the overall availability of new credit for companies nowadays?

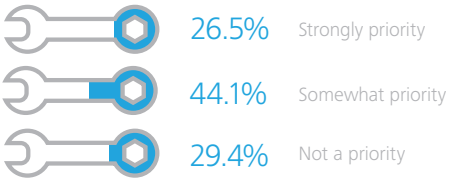


Graph 9: In your view how are financing costs for companies in your country likely to change over the next 12 months?



BiH CFOs also expect business remodelling or restructuring to be a priority in the next 12 months (71%). This is consistent with their cost-reduction strategies and focus on the better use of available resources. 53% of BiH CFOs believe that mergers and acquisitions will increase over the next 12 months, which to a certain extent aligns with the latest trends across Europe. On the other hand, 37% expect M&A activities to remain unchanged while 10% expect a decrease.

Graph 10: To what extent is business remodelling or restructuring likely to be a priority for your business over the next 12 months?

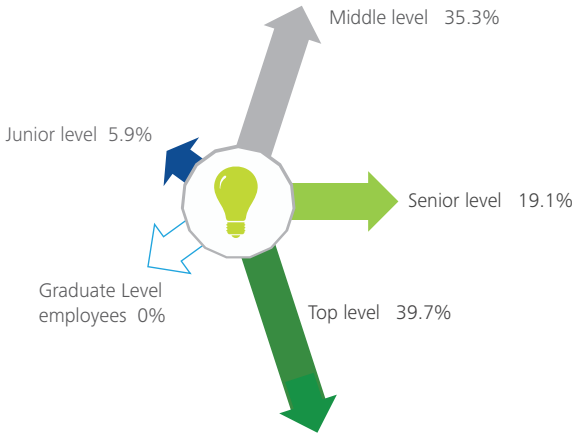


Bank borrowing remains a more attractive source of financing than equity raising.

The availability of financial talent

More than a third of BiH CFOs expect talent shortages in the finance area over the next year. These shortages are mostly expected at middle (up to five years of experience) and most senior management levels.

Graph 11: Where do you expect significant shortages in talent in finance over the next year?



Central European economic and business overview

“May you live in interesting times...”

Introduction

The famous old Chinese curse “May you live in interesting times” has a powerful grip on the economies of Central Europe (CE) as the region’s CFOs strive to steer their companies to ultimate success through the obstacles of uncertainty, volatility and rapid global economic change.

But in interesting times, winning financial strategies depend more than ever on timely and relevant information. That’s why we’re so pleased to publish this report including the CE CFO Confidence Index, which summarises the perspectives of around 600 CFOs from 13 countries across Central Europe. While we all have daily access to abundant (and often conflicting) forecasts from analysts, academic economists, journalists and politicians we believe it’s just as valuable to understand what practicing CFOs have to say.

The shift of business impetus from the developed to the developing world has been seen as the principal driver of global change over the last decade. That said, the current re-industrialisation of the US and the deceleration in developing countries suggests the picture is not as clear-cut as believed. So the big question for business leaders in Central Europe is: “Can the region grow into one of the new centres of economic influence?”

We don’t attempt to provide a definitive answer in this report. Rather, building on past editions, we try to show how short-term plans and expectations are evolving to give the region’s largest companies a context for their decision-making. In this way, we hope to contribute to their success and so help the region exert the greater gravitational pull to attract business influence to CE.

The good news is that optimism for company prospects has become more widespread than pessimism over the six months since the last survey. On the down side, the majority of CE CFOs believe the time has not yet come to take more risk on to company balance sheets. The key business priority for CFOs might sound simple: to increase revenues. But, in the interesting times we are experiencing in Central Europe, simple does not translate into easy-to-achieve.

Key findings

- The CE CFO Confidence Index shows signs of optimism among nearly 600 CFOs from companies across 13 countries, which are experiencing volatility and external financial uncertainty
- Despite signs of optimism, the majority of CFOs in Central Europe believe that the time has not yet come to take more risk on to company balance sheets
- CFOs in CE hold divergent views on their priorities for the next 12 months
- Many CFOs plan to reduce gearing levels, associated with a corresponding expectation of higher financing costs
- While talent shortages are not of concern to most participating CFOs, there are opportunities for experienced financial professionals around the region
- The top priority for next year, shared by many CFOs in Central Europe, is simply to grow their revenues

About the fifth CE CFO Survey

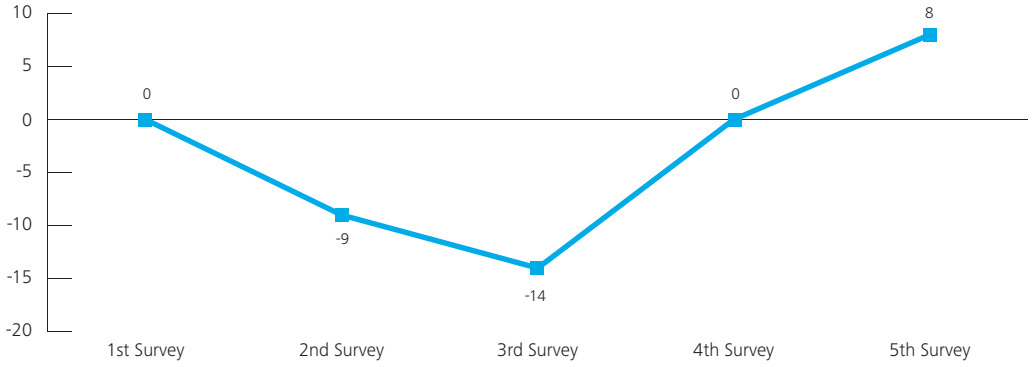
The report compares the expectations of CFOs from 13 Central European economies (Albania and Kosovo, Bosnia and Herzegovina, Bulgaria, Croatia, the Czech Republic, Hungary, Latvia, Lithuania, Poland, Romania, Serbia, Slovakia and Slovenia). It is based on the answers of 580 CFOs from a broad range of industries who responded to our survey in October and November 2013. The survey captures shifts in CFOs' opinions on factors including risks, GDP growth and financing priorities. It has become a benchmark for agile decision-making that takes into account the financial attitudes of major corporations across Central Europe.

About the author

This part of the report was prepared by Dr Michał Zdziarski, Research Director, Warsaw University Executive MBA, exclusively for Deloitte Central Europe. Dr Zdziarski's research interests include strategy, finance, leadership and international business.

Signs of optimism

Graph 1: CE CFO Confidence Index



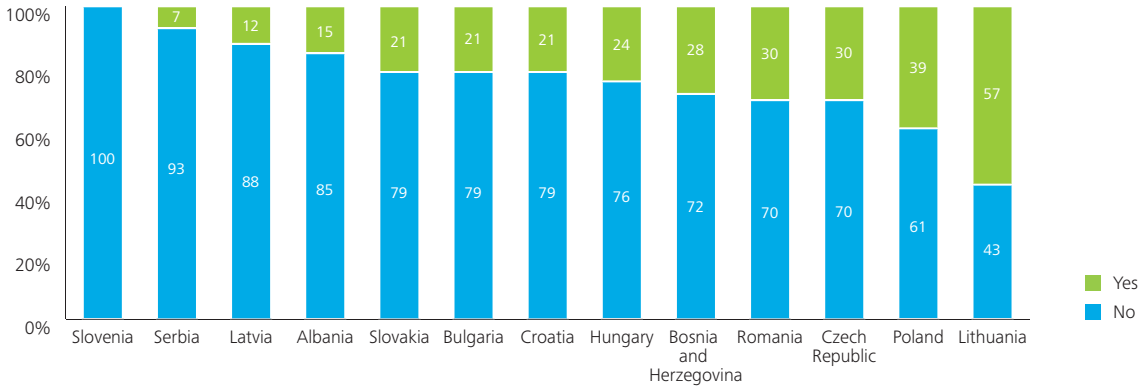
We have developed the CE CFO Confidence Index[1] to track the evolution of CFO sentiments regarding their companies' financial prospects across many sectors and geographies. We have taken into account accumulated opinions from five major economies in the region: Poland, the Czech Republic, Romania, Hungary and Slovakia, which jointly represent close to 80% of CE's aggregated GDP. We have weighted the influence of CFOs' sentiments from different countries by the relative size of their economies, to best represent the overall expectations for changing regional dynamics.

The 22-point increase in the CE CFO Confidence Index between the third and fifth editions signals the growing optimism of the region's finance professionals. The level of confidence now is the highest of all editions of the survey we've undertaken since its launch in June 2011, into a region that was already affected by the global slow down. Therefore, we propose to conservatively interpret the current levels of CFO confidence as a sign of cautious optimism.

[1] The CE CFO Confidence Index is calculated based on net optimism – the difference between the percentage of CFOs who are optimistic about the financial prospects for their company compared with six months ago and those who are pessimistic, weighted by the proportion who believe that conditions remain unchanged. We calculate the index based on results from five major economies of the Central European region, which between them have a 78% share of the total GDP of all analysed countries. Net optimism is then weighted by product of individual country (GDP) to produce the index for the overall region. The results from the first Deloitte CE CFO Confidence Index are taken as base data.

Staying on the safe side

Graph 2: CFO views on whether this a good time to take greater risk on to company balance sheets

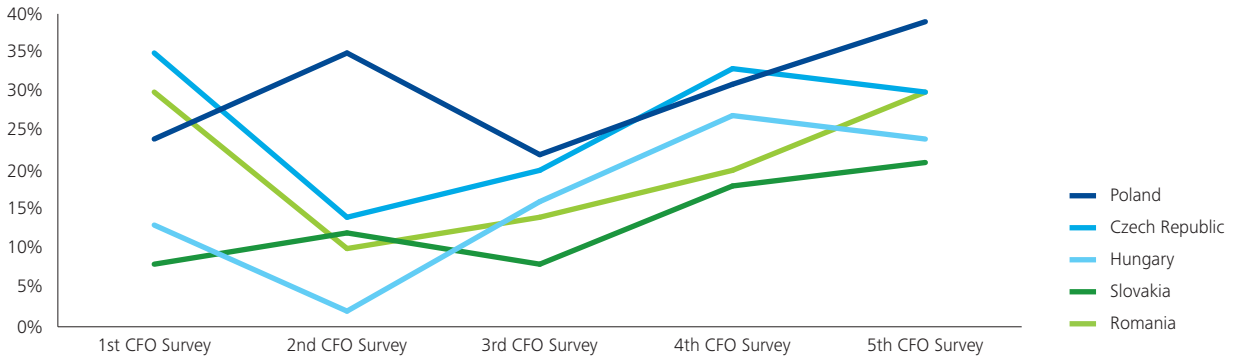


The majority of CFOs in all countries except Lithuania believe that now is not the time to take greater risks on to company balance sheets. The diversity of opinion on risk-taking across the region is notable: in Slovenia, no CFOs at all believe that their company should increase its risk exposure; 57% of Lithuanian CFOs, meanwhile, are willing to leverage their growth potential. It is also worth noting the relatively high proportion of CFOs who appear ready to take more risk in the three largest economies of the region: Poland (39%), the Czech Republic (30%) and Romania (30%). These countries' combined share of the total GDP of the Central European region is over 60%, and there is a corresponding difference in the size of the business operations of our respondents. In the two following countries, fewer CFOs are willing to increase risk levels – Hungary at 24%, and Slovakia at 21%.

Results across Central Europe are far from the six-year high in optimism expressed by UK CFOs. With 54% of them bullish about taking greater risks, Ian Stewart, Chief Economist at Deloitte, expects UK corporations to significantly increase their capital expenditure over the next 12 months.

[2] The Deloitte CFO Survey UK. 3rd Q results.

Graph 3: Percentage of CFOs choosing now is a good time to take greater risk on to company's balance sheets

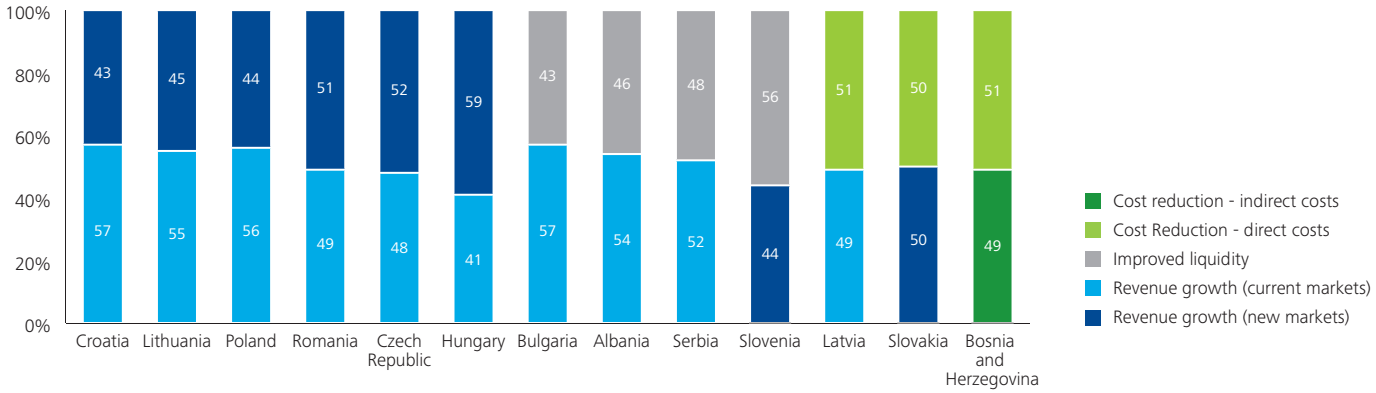


Comparing the risk-aversion findings across all five editions of the Deloitte CE CFO Survey, we can see that the proportion of CFOs in Poland, Hungary and Slovakia that believe now is a good time to take greater risk on to the balance sheet has increased by more then 10% since the first survey in June 2011. In Romania the proportion has returned to the 30% level that we also saw in the first survey. This recovery follows a steep decrease in the second edition, to only 10% of Romanian respondents. The Czech Republic is the only country where the proportion of CFOs willing to take greater risks has decreased; it has fallen by close to 5% over last two and a half years, while remaining on the relatively high level of 30%.

The overall trend from the five largest countries is towards an increased proportion of CFOs who are willing to take more risks. Maybe the time to increase risks has not yet arrived, but we are getting closer to a more endemic mood of expansionary investment. In interesting times like the present, it is necessary to make a decision: should we take greater risk now, hoping to maximise the benefit of grabbing investment opportunities ahead of the curve? Or should we instead take a conservative approach and minimise the chance of making losses if the trend goes into reverse?

Regional view – divergent needs, different priorities

Graph 4: Company business focus over the next 12 months. Top two priorities



Comparing the top priorities for CFOs over the next 12 months by country, we see three distinct groups, which we have called:

- Growth-seeking
- stability-seeking
- cost advantage-seeking

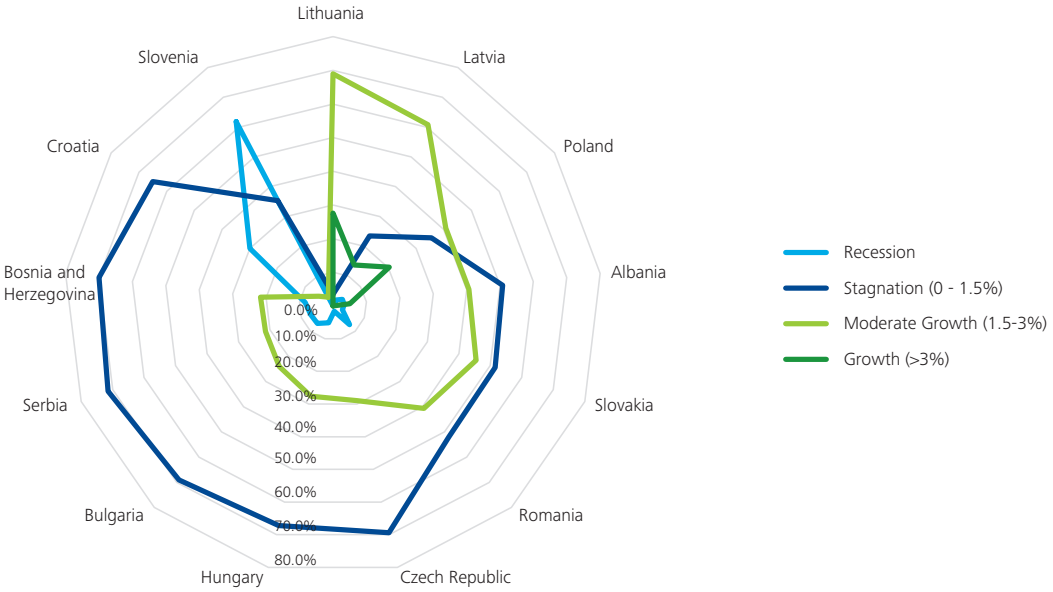
CFOs' top priorities in growth-seeking countries are almost equally divided between two revenue-growth alternatives: growth from current markets or from new ones. The growth-seeking group of countries is the most numerous and includes the largest economies in the region: Poland, the Czech Republic, Romania and Hungary as well as Croatia and Lithuania. In these countries factors like austerity, cost control and improving liquidity are out, and expansion priorities are clearly in.

In the next group of countries, all located in the south of the region, improving liquidity is one of the two top priorities. While seeking revenue in current markets is the primary challenge in Bulgaria, Albania and Serbia, this might be hard to achieve – CFOs expect stagnation in all these markets. Even more challenging might be growing revenues from new markets, which is the second priority for CFOs in Slovenia. Their expectation of recession in their home market leaves them with no other alternative.

The group of countries seeking cost advantage is the least homogeneous, as indirect cost reduction is accompanied by three disparate priorities: revenue growth from existing markets in Latvia; direct cost reduction in Bosnia and Herzegovina; and revenue growth from new markets in Slovakia.

It's all about growth

Graph 5: CFOs' expectations for their countries' GDP growth in 2014



In general, CFOs report that where growth is currently weak or absent, the situation is not expected to reverse in any dramatic way. Some signs of improvement are expected by CFOs operating in four countries – Lithuania, Latvia, Poland and Albania – where the dominant best estimate is for moderate annual growth of between 1.5 to 3% of GDP. In these four countries alone, relatively small groups of CFOs expect growth to exceed 3% in 2014.

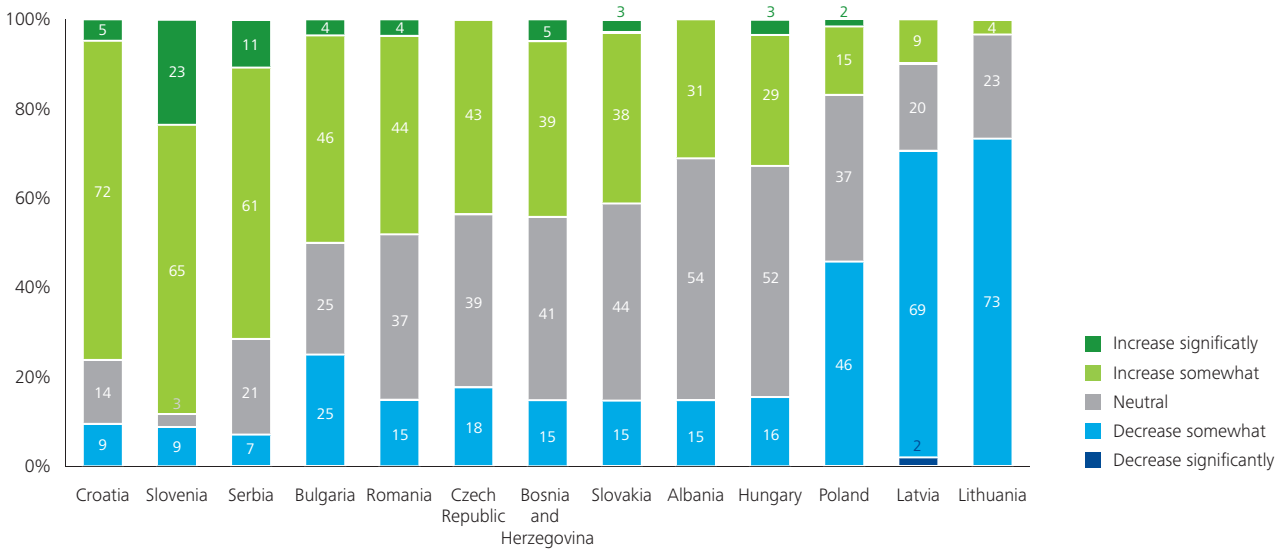
The dominant expectation for the region is stagnation (between 0 and 1.5%), chosen most frequently by CFOs in nine countries. Recession is clearly the consensus view for Slovenian economic prospects in 2014.

Overall, therefore, the region's waters of economic prosperity remain unsettled. It will be critical to learn in the next few months what would be more transferable among countries in the region – the moderate economic growth expected in Poland, Latvia and Lithuania, or the recession that Slovenia is going through.

The prospects for employement

GDP growth is again the key factor when we look at expected changes in unemployment. The expected moderate growth in Lithuania, Latvia and Poland corresponds with anticipated decreases in the levels of unemployment in these three countries. In all other countries, CFOs expect fewer opportunities for job seekers and current employees. In Slovenia, which remains in recession, the largest proportion of CFOs expect a significant increase in unemployment levels, and any expectations of a significant increase in employment will need to wait for GDP to grow faster than 3%.

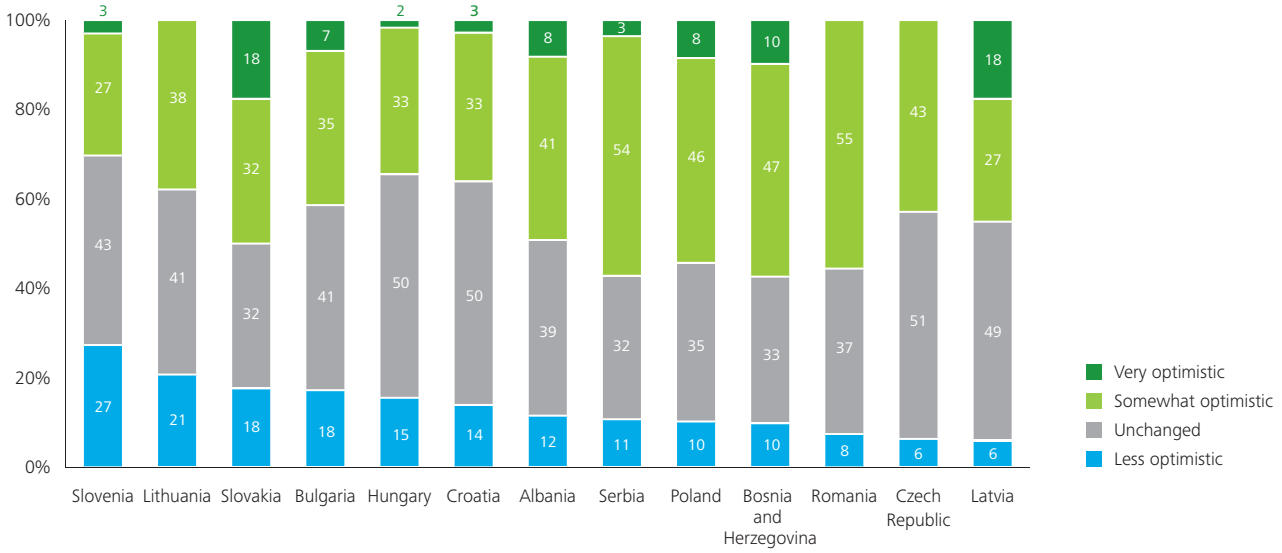
Graph 6: How CFOs expect levels of unemployment to change in their countries over the next 12 months



Financial prospects compared to six months ago

CFOs are much more optimistic about their own companies' prospects in the next six months than for the GDP growth outlook of the countries in which they are located. In all countries, more CFOs have become more optimistic about their company prospects in the next six months than have become less optimistic. Even in troubled Slovenia, expectations of continuing recession do not translate into pessimistic views on companies' financial prospects; this is perhaps thanks to growth from new markets and exports that might compensate for the weakness of the domestic market. In several markets, there is a net difference of over 40% between 'very/somewhat optimistic' CFOs and their less optimistic peers. These countries include Poland, Romania and Serbia, as well as Bosnia and Herzegovina. CFOs have clearly learned to operate their companies in stagnant, troubled economies.

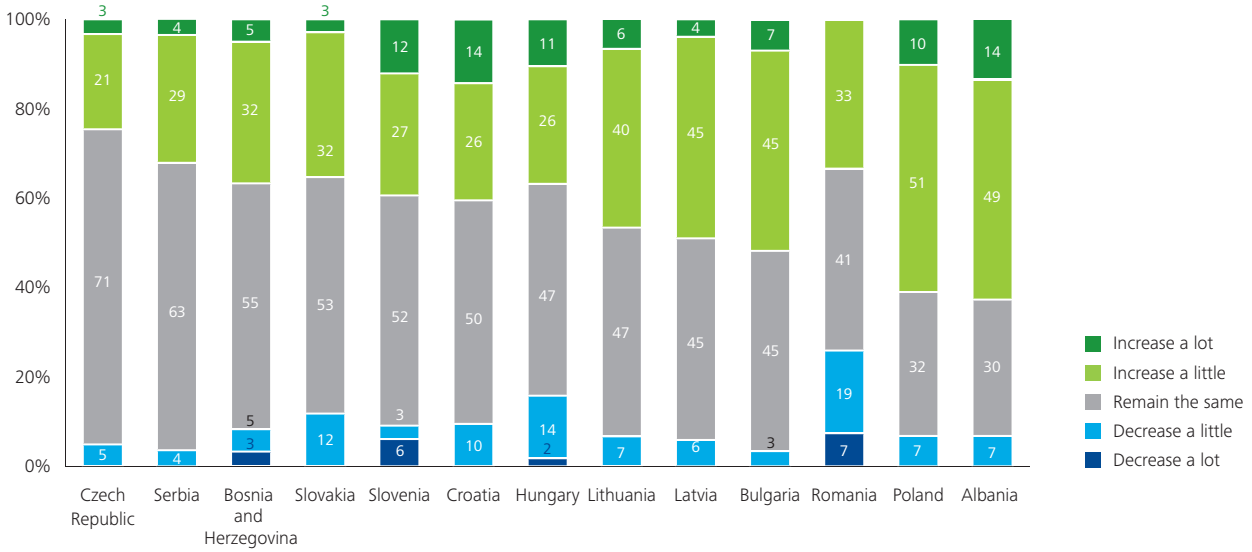
Graph 7: CFOs' views on their companies' financial prospects compared with six months ago



Financial prospects – the long-term view

Most CFOs predict no change in their ability to service their debt, while almost the same proportion expect a moderate improvement over the next three years. Radical changes in companies' financial performance were indicated only rarely, suggesting that current long-term views on companies' financial prospects are in fact closer to the expected changes in GDP than they are to anticipated short-term improvements in companies' financial performance. While there are notable exceptions of companies implementing a winning strategy in a difficult environment, no company is isolated from its business context. For the majority of CFOs, therefore, the long-term prospects of their companies are grounded in the dynamics of the external environment.

Graph 8: How CFOs expect their ability to service debt to change over the next three years

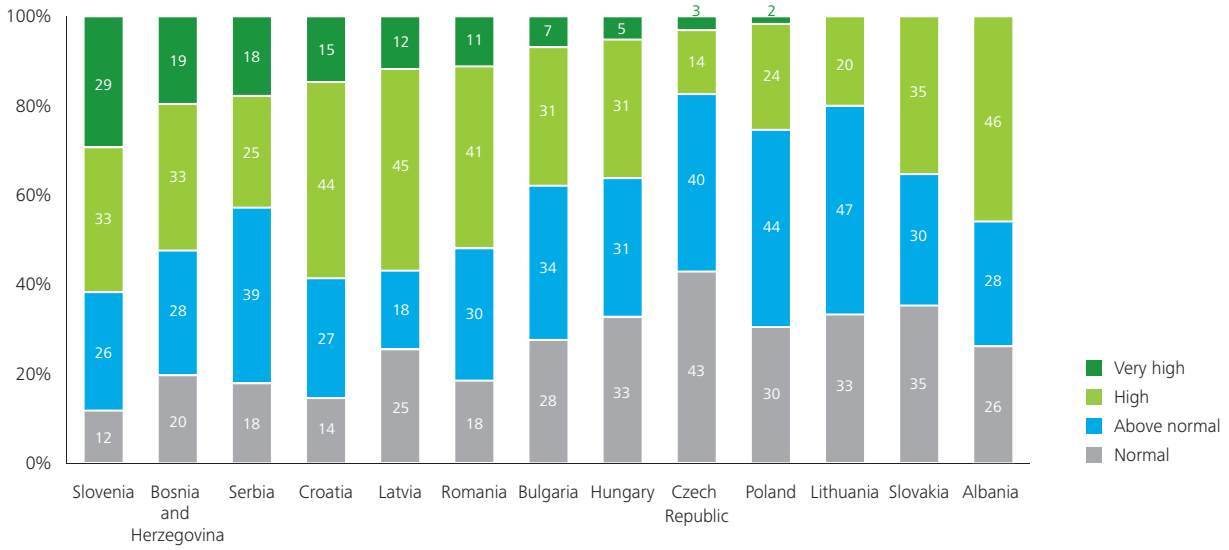


External financial uncertainty – learning to cope with the "New Normal"

The majority of CFOs in the region describe the general level of external financial uncertainty as above normal, high or very high. This majority is as high as 88% in Slovenia and 70% in Poland. This suggests that they do indeed operate in interesting times, when higher uncertainty becomes part of the "new normal" environment.

Many companies react to the situation by withholding investment funds and focusing on quick wins. While this strategy is typical of how to deal with cyclical downward shifts in the economy, there is less clarity about how to manage financial risks in an environment where high levels of external financial uncertainty are normal for the long term.

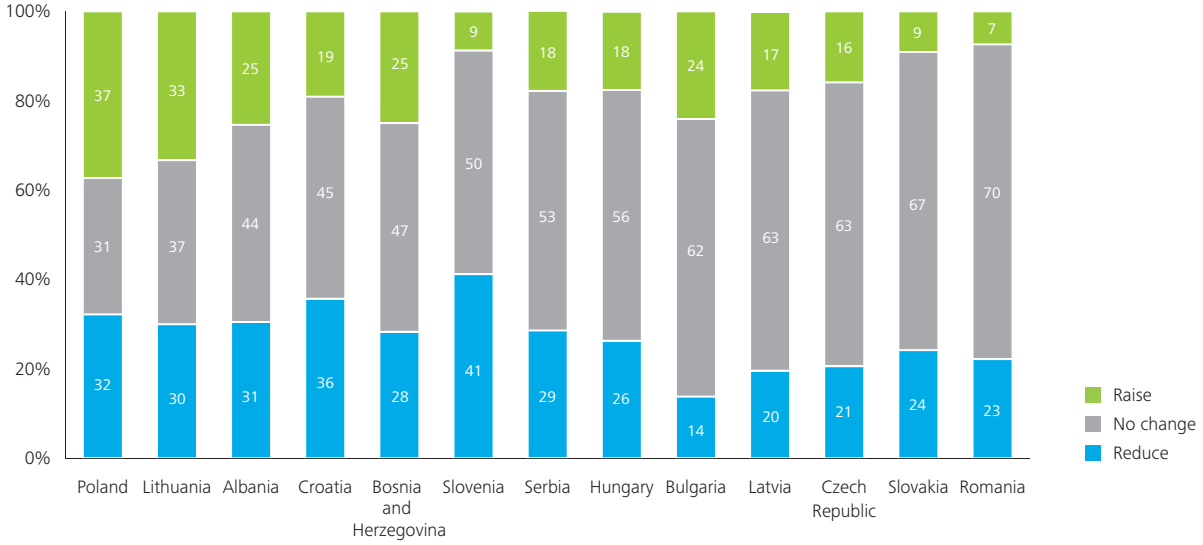
Graph 9: CFOs' opinions on the general level of external financial and economic uncertainty facing their businesses



Gearing and costs of finance

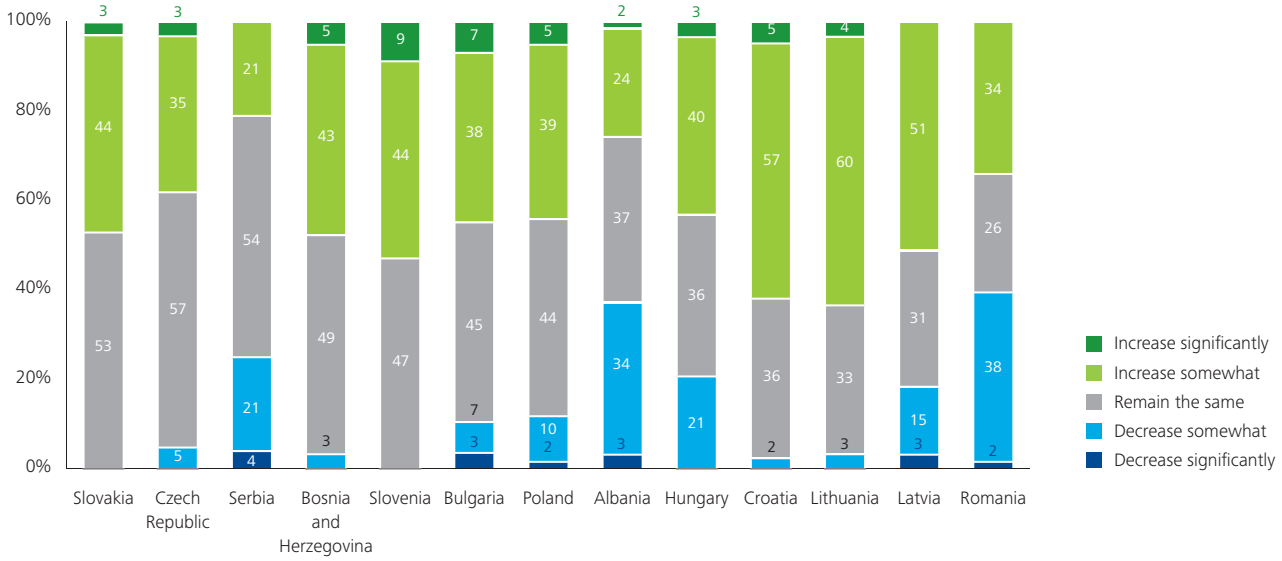
Most CFOs remain cautious on the subject of gearing. In seven markets, the clear majority anticipate no change, and in all countries except Poland the largest proportion of CFOs choose this option. The fact that Poland and Lithuania have the largest proportion of CFOs anticipating that gearing will increase corresponds with these two countries also having the highest proportion of CFOs who say that now is a good time to take greater risks on to the balance sheet. Efforts to reduce gearing will be more common among CFOs based in the southern part of Central Europe: in the troubled economy of Slovenia, as well as in Croatia, Bosnia and Herzegovina, Serbia, Albania and Hungary, plans to reduce gearing are quite common. Overall, reducing gearing is the second most popular strategy after "no change".

Graph 10: How CFOs anticipate their levels of gearing to change over the next 12 months



Central European CFOs feel that the costs of finance are set to remain the same or to increase somewhat. There are four exceptions, Romania, Albania, Hungary and Serbia, where between 39% and 21% of CFOs believe that interest rates are likely to decrease somehat over the next 12 months. Expectations of a significant increase are marginal – the 9% of Slovenian CFOs who expect such a change is the largest group among the entire sample.

Graph 11: How CFOs expect the costs of finance for companies in their countries to change over the next 12 months

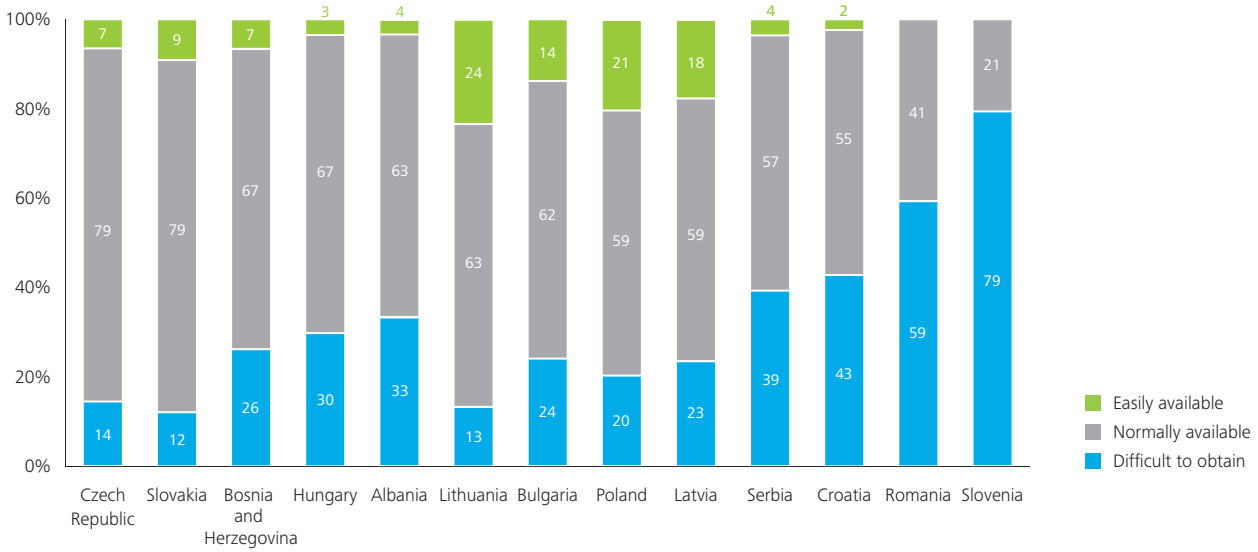


Availability of new credit

Most CFOs in our survey see new credit as "normally available". The story is different in Slovenia and Romania, where 79%, respectively 60%, of CFOs have difficulties in accessing credit. Compared to last year, credit availability has improved notably in Hungary, and it is less of an issue even to 8% of Slovenian CFOs than it was then.

While 6% more Polish CFOs than last time find credit easily available, 5% also find it more difficult to obtain. Such results suggest that the region's largest economy is set for an increase in those companies using M&A activity to restructure and seek new efficiencies.

Graph 12: How CFOs rate the overall availability of new credit for companies

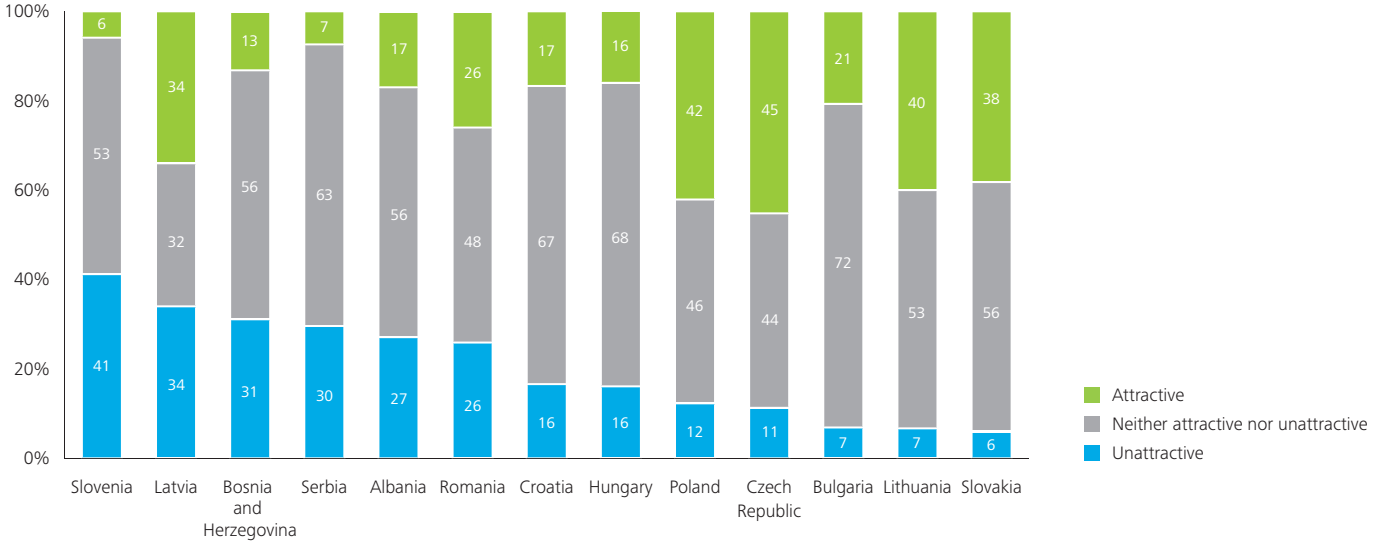


Funding alternatives

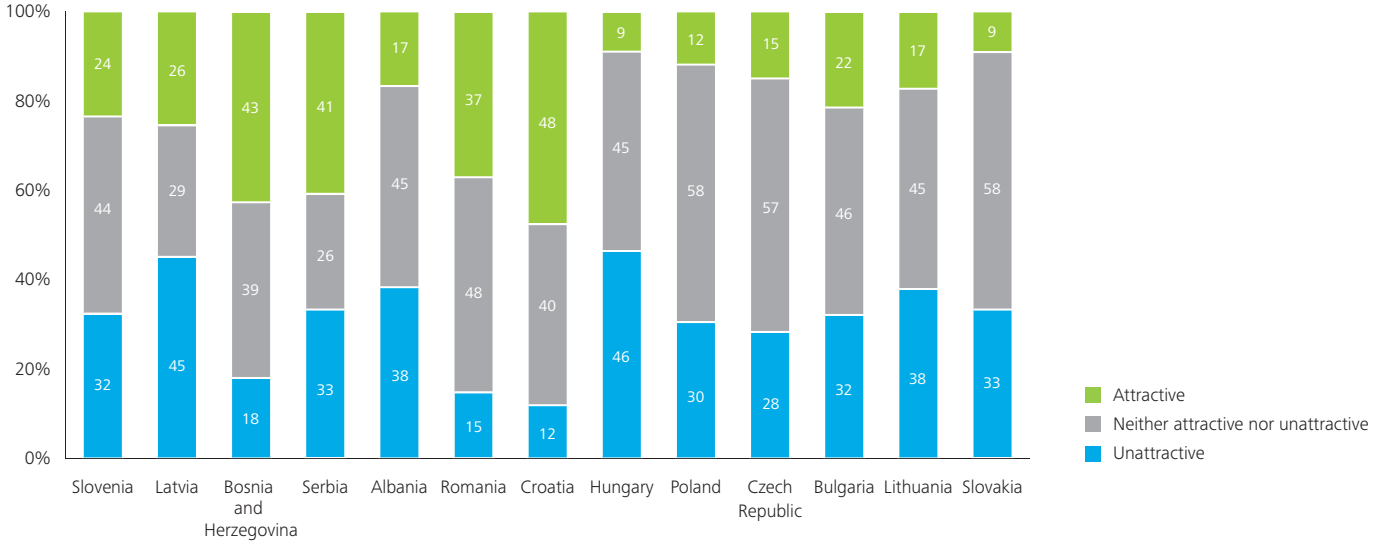
There is quite a diversity in the perceived attractiveness of bank borrowing versus equity finance among CE countries. In Poland, the Czech Republic and Slovakia, CFOs regard equity raising as a less attractive option for funding their plans than bank borrowing.

The opposite holds true for CFOs from Serbia, Bosnia and Herzegovina, Slovenia, Croatia and Romania – countries where availability of new credit is often more restricted. In the remaining three countries, there is a less clear-cut orientation towards bank credit rather than equity raising.

Graph 13: Currently, CFOs believe bank borrowing as a source of funding is:



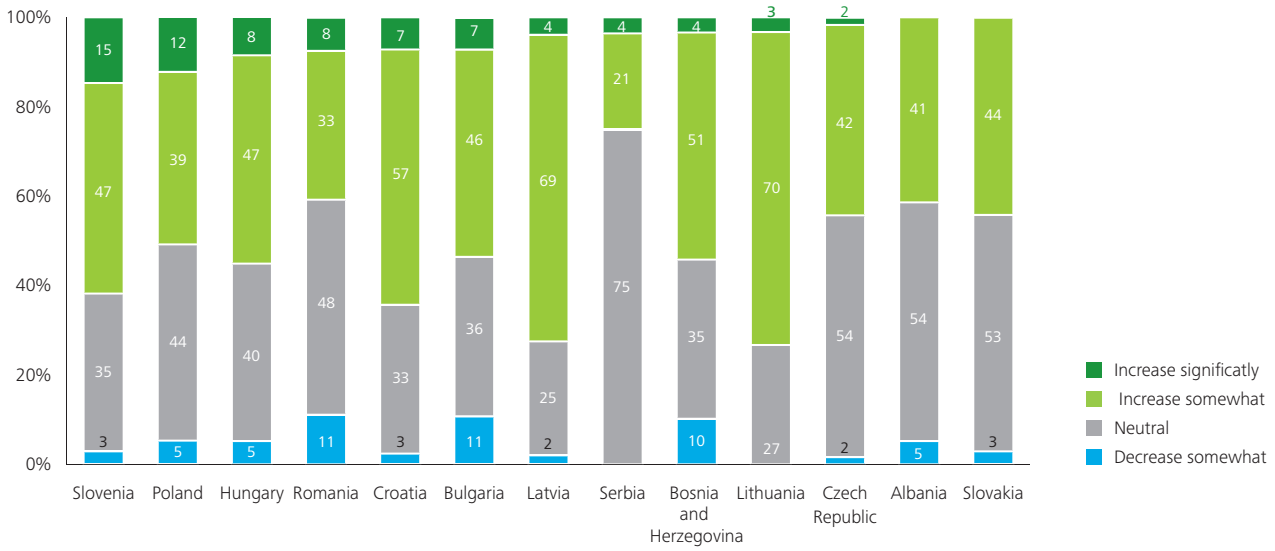
Graph 14: Currently, CFOs believe raising equity as a source of funding is:



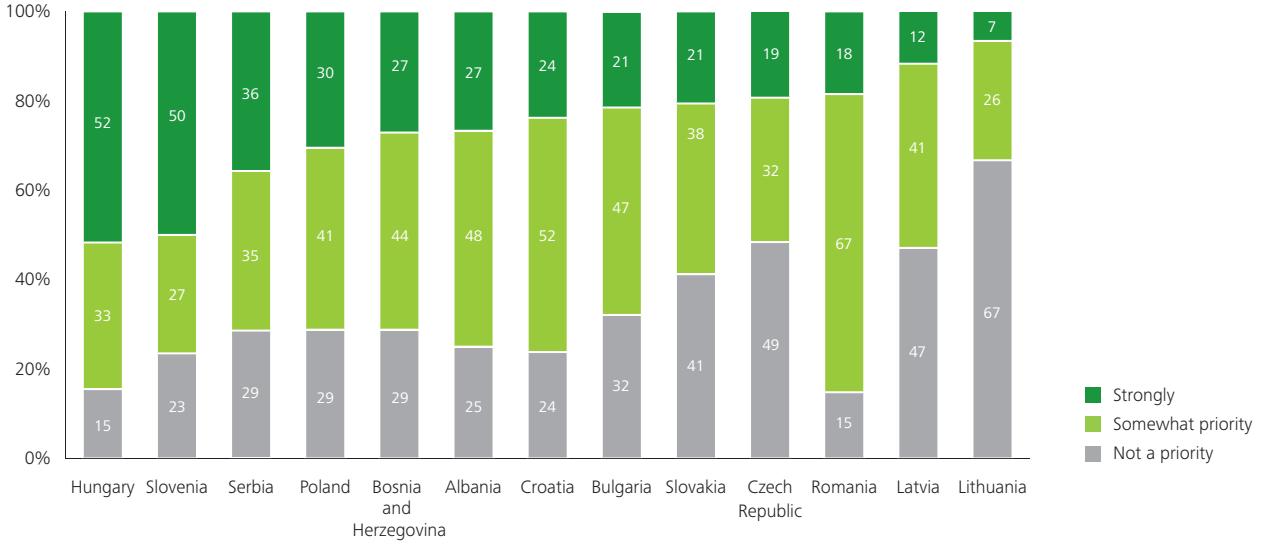
Mergers, restructuring and remodelling

CFOs will lead a great deal of restructuring/remodelling and M&A over the next year. Restructuring/remodelling will be strong priority for more than 50% of CFOs in all countries except Lithuania, where expected growth is not necessitating major internal efficiency initiatives. This level of restructuring/remodelling is impressive, as much has already been done in most CE markets in the last few years. The expected increase in M&A activities in most markets is another means of seeking efficiency savings in times where the simple goal of revenue growth can be difficult to achieve organically. Slovenia and Poland, currently at very different stages of the economic growth cycle, will see much activity in both mergers and restructuring.

Graph 15: How CFOs expect levels of M&A activity to change in their countries over the next 12 months



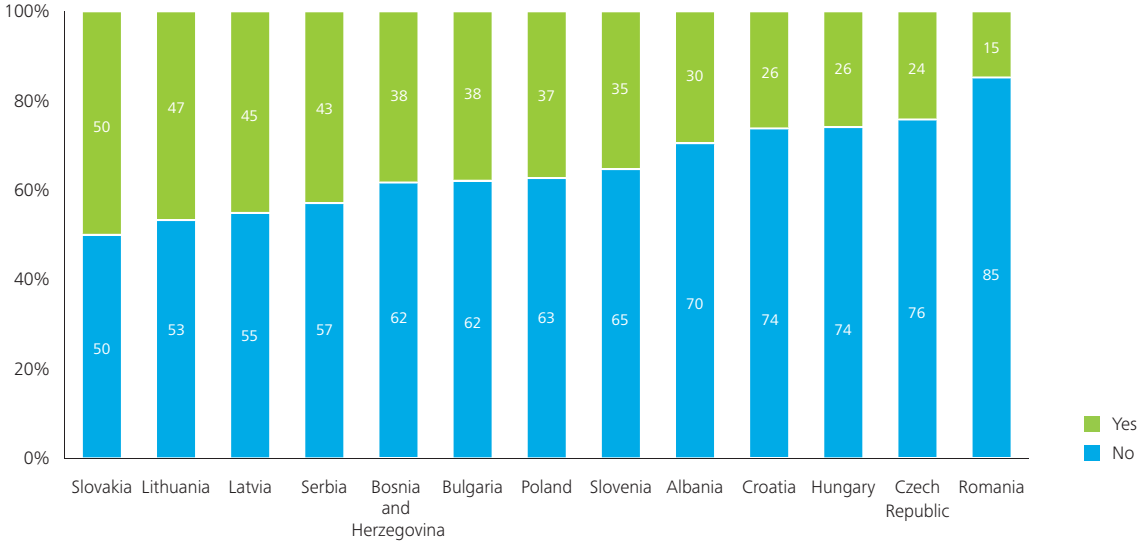
Graph 16: To what extent business remodelling or restructuring is likely to be a priority over the next 12 months



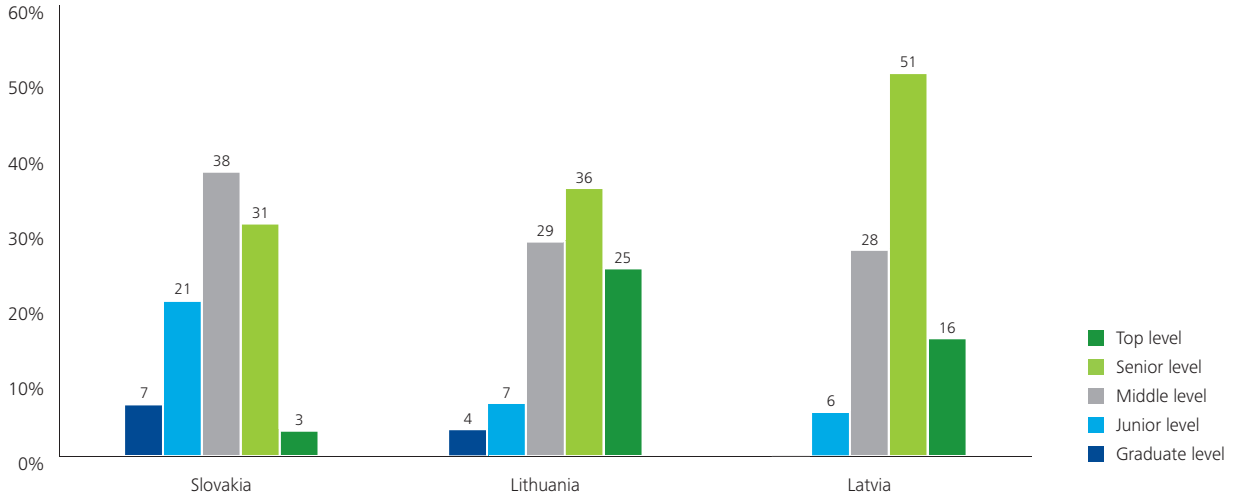
Talent shortages and prospects for finance professionals

The majority of CFOs in the region do not expect any talent shortages in financial roles. There is a considerable variation in views, however, with some promising prospects for experienced finance professions in Slovakia, Lithuania and Latvia where middle and senior-level finance executives are more in demand than in any other country in Central Europe.

Graph 17: Whether or not CFOs expect talent shortages in the finance area over the next year



Graph 18: Expected talent shortages in finance over the next 12 months - top 3 countries



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Methodology

The CE CFO survey took place in October & November 2013. A total of 580 CFOs across 13 countries completed our survey. The survey is divided into two parts, first - local analysis based on responses from Bosnia and Herzegovina and the second part is based on all the responses across the region. Not all survey questions are reported in each annual survey. If you were interested to see the full range of questions, please contact acofek@deloittece.com.

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 organization rates among peers.