CFO Signals™

What North America's top finance executives are thinking – and doing

High-Level Report

2nd Quarter 2013

CFO Signals

About the CFO Signals survey

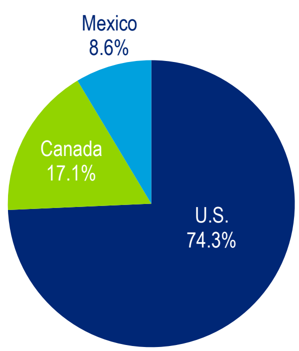
Each quarter, *CFO Signals* tracks the thinking and actions of CFOs representing many of North America's largest and most influential companies. This is the second quarter report for 2013.

For more information about the survey, please see the methodology section at the end of this document or contact nacfosurvey@deloitte.com.

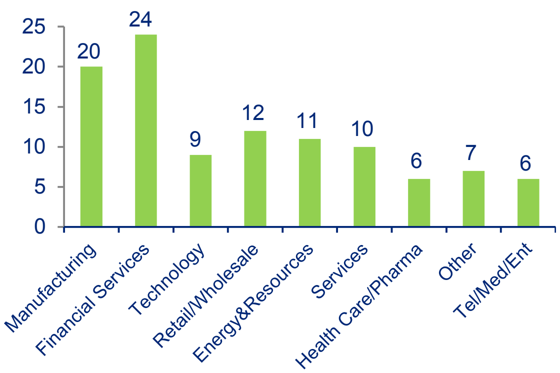
Who participated this quarter?

One hundred and five CFOs responded this quarter. Seventy percent of the CFOs are from public companies, and 80% are from companies with more than $1B in annual revenue.

Participation by Country



Participation by Industry



IMPORTANT NOTES ABOUT THIS SURVEY REPORT:

All participating CFOs have agreed to have their responses aggregated and presented.

Please note that this is a "pulse survey" intended to provide CFOs with quarterly information regarding their CFO peers' thinking across a variety of topics. It is not, nor is it intended to be, scientific in any way, including in its number of respondents, selection of respondents, or response rate, especially within individual industries. Accordingly, this report summarizes findings for the surveyed population but does not necessarily indicate economy- or industry-wide perceptions or trends. Except where noted, we do not comment on findings for segments with fewer than 5 respondents. Please see the Appendix for more information about survey methodology.

Additional findings available in full report
(please contact nacfosurvey@deloitte.com for full report)

- Detailed findings (by industry)
- Industry-by-industry summaries
- Country-by-country summaries

Findings at a Glance

Business Environment

Which external factors will most spur and impede companies' performance over the next year? Even more than last quarter, CFOs say the most positive factor helping companies grow is the status of North American economies. Top impediments to growth center heavily on public policy, with increasing concerns about environmental regulation. **Page 8.**

How do CFOs regard the current and future health of some of the world's major economies? CFOs are feeling reasonably good about North America and China, but expectations for Europe are dour. More CFOs rate North America's economic health as good than as bad, and nearly two-thirds are optimistic about the region's trajectory. By comparison, 53% are optimistic about China, and just 14% are optimistic about Europe. **Page 9.**

How concerned are CFOs about international expansion risks? CFOs say they are concerned about governments' increasingly aggressive efforts to tax foreign companies' profits, about taxes on passive income, and about taxes on repatriated earnings. **Page 10.**

With U.S. equity markets up around 17% for the year, what do CFOs think about valuations? CFOs believe equity valuations are too high – except when it comes to their own companies. Nearly 60% of CFOs think U.S. equities are overvalued, and only 4% think they are undervalued. About 39% of CFOs believe their company's stock is undervalued, and only 11% say it is overvalued. **Page 11.**

Company Priorities and Expectations

What is the business focus for companies over the next year? Even more than last quarter, the vast majority of CFOs say their companies are focused on pursuing opportunity over limiting risk, and much more on growing and scaling than on contracting and rationalizing. Notable this quarter is an increasing bias toward new offerings, new geographies, and rising capital investment. **Page 12.**

What do companies plan to do with their cash over the next year? CFOs say their top uses of cash will be investments in organic and inorganic growth – well ahead of alternatives like funding operational improvement efforts and holding cash as a risk hedge. What they don't dedicate to growth investments will mostly be used to pay down debt, buy back stock, and pay dividends. **Page 13.**

Which external and internal risks are top of mind for boards? Boards' chief external concerns are economic health in North America and Europe, the effects of slow growth on competition, and governments' regulatory activity. Internally, boards are less worried about the quality of strategy than they are about having strategy reflected in investments and operations. **Page 14.**

Company Priorities and Expectations (continued)

What have companies done to reinforce their risk management approaches over the past five years? Companies have taken strong steps to improve risk awareness, clarify responsibility, and plan for risk events. The dominant focus has been on operational risk, but CFOs say they have also gotten much more aggressive about financial risks. **Page 15.**

To what degree are companies managing their retirement risk? Since our 4Q11 survey, companies have gotten considerably more aggressive about de-risking their retirement liabilities. Nearly two-thirds of companies have tried at least one de-risking tactic, and the average number of tactics employed has expanded. **Page 16.**

How do companies expect performance, spending, and hiring to change over the next 12 months? Growth and profitability expectations remain modest this quarter, with sales growth expectations only slightly higher at 5.7% (still below the 7% long-term average) and earnings growth lower at 10.3%* (well below the 12.3% historical average). Capital spending growth expectations declined to 7.5%*, but dividend growth rose to 4.5%* (well above their longer-term average). Domestic hiring growth expectations improved to a still-muted 2.4% (the U.S. sits at just 1.3%, and 21% of all CFOs still expect cuts). **Pages 17-19.**

How does CFOs' optimism regarding their companies' prospects compare to last quarter? CFO optimism continued to rebound this quarter, rising from a strong +32 last quarter to an even stronger +46 this quarter. Nearly 60% of CFOs express rising optimism, and just 13% express rising pessimism (the lowest proportion in the three-year history of this survey). **Page 20.**

Overall, what external or internal risk is of most concern? Over the past few quarters, CFOs' top worries have become less about specific events (e.g. recessions, collapses, and legislation) and more about longer-term lack of improvement. They appear more worried about worldwide economic recovery and growth (and less worried about specific economies), and they express more concern about the impacts of fiscal policy on longer-term economic health (and declining concern about the effects of specific taxing and spending policies). **Page 21.**

Personal Priorities

Which financial, investment, operational, and valuation measures have the strongest impact on CFO pay? Profitability is still king, with more than 95% of CFOs reporting substantial impact on their compensation. Economic measures (i.e., those incorporating both income statement and balance sheet measures) are next at 70%, and nearly two-thirds say growth metrics have a substantial impact. **Page 22.**

*All numbers with an asterisk are averages that have been adjusted to eliminate the effects of stark outliers.

Summary

An air of optimism

On the face of things, this quarter seems a lot like the last. Companies are performing relatively well, but they're still doing it mostly through tight cost management and intense business focus – and not by riding waves of growing customer demand.

The most acute risks in Europe and the U.S. still appear averted, but Europe remains dragged down by tight credit and balance sheet repair. Growth in North America and China, while relatively steady, has not been strong enough to markedly bolster domestic hiring or investment. And CFOs are still wary of the near- and long-term effects of monetary, fiscal, and regulatory policy worldwide.

But despite all these similarities, this quarter feels notably different. CFOs' responses this quarter seem to indicate an air of optimism that has been mostly absent for well over a year. Perhaps the best news is that CFOs mostly see North America's economies as healthy, and they are particularly bullish about where they will be next year. And at a company level, more are positive about their own prospects than has been the case since the first quarter of 2012.

But also apparent in this quarter's findings seems to be the notion that, even though their appetite for risk and growth is increasing, companies' approaches will be as measured and methodical as those that have helped them preserve earnings over the past several years. Continued reluctance to accelerate longer-term investments and a maintained focus on shoring up key risks both serve as reminders that downside risks are still a strong concern and that flexibility remains a valued asset.

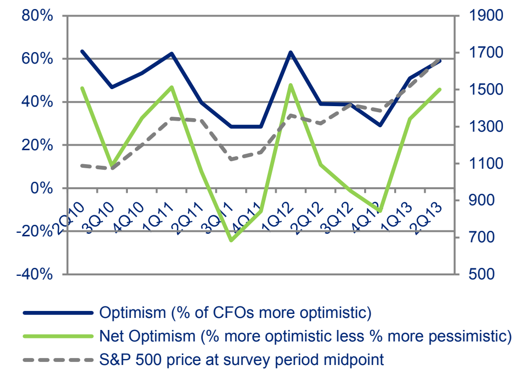
Signs of life

Notwithstanding their continuing concerns, the signs that CFOs and their companies are feeling less wary and more confident are pervasive in this quarter's survey results. CFO optimism continued to rebound, rising from a strong +32 last quarter to an even stronger +46 this quarter. Nearly 60% of CFOs express rising optimism, with just 13% expressing rising pessimism (the lowest proportion in the three-year history of this survey).

Companies' rising optimism is spilling over into their strategic plans. Even more than last quarter, the vast majority of CFOs say their companies are focused on pursuing opportunity over limiting risk, and much more focused on growing and scaling than on contracting and rationalizing. Moreover, CFOs say the top two uses of cash in 2013 will be investments

Own-Company Optimism

CFO optimism relative to previous quarter



Since the 1Q13 survey…

- S&P 500 up almost 10% (again); earnings strong, but sales not as strong
- Eurozone in sixth quarter of recession; Cyprus economy emerged as troubled
- Increased debate of austerity pros/cons; talk of sequestration rework/cancellation
- Continuing housing market rebound

in organic and inorganic growth – well ahead of alternatives like funding operational improvement efforts and holding cash as a risk hedge. What they don't dedicate to growth investments will be mostly used to pay down debt, buy back stock, and pay dividends – not actions generally associated with strong concerns about the future.

The primary cause of rising optimism seems to be CFOs' perception of the North American economies. Nearly 30% of CFOs rate the region's economic health as more good than bad, and just 9% rate it as more bad than good. Moreover, nearly two-thirds of CFOs are optimistic about the trajectory of North American economies; by comparison, 53% are optimistic about China, and just 14% are optimistic about Europe.

Not there yet

Although nearly three-fourths of CFOs say North America's economic progress is the business environment's most positive force for growth, they also overwhelmingly say U.S. equity markets (which are up about 17% year-to-date) are over-valued, and their growth and profitability expectations remain modest. Sales growth expectations are only slightly higher this quarter at 5.7% (still below the 7% long-term average), and earnings growth declined to 10.3%* (well below the 12.3% historical average).

* All numbers with an asterisk are averages that have been adjusted to eliminate the effects of stark outliers.

+ Note that net optimism, as calculated, does not explicitly account for the level of "no change" responses.

Summary (cont.)

Modest growth expectations are continuing to take a toll on investment. At 7.5%, capital spending growth expectations are below their long-term survey average, and domestic hiring growth expectations are still muted at 2.4% (the U.S. sits at just 1.3%, and 21% of all CFOs expect cuts). Instead of committing to these longer-term investments, CFOs say their companies are more likely to give cash back to shareholders; dividend growth expectations reached their highest level in nearly three years, and share buybacks are expected to be one of the top uses of cash for 2013.

Underlying these expectations are lingering concerns about the actions of governments worldwide. CFOs name fiscal, regulatory, and environmental policy as their top three growth impediments overall, (economic stagnation and competitive pressures are next), and companies considering growth outside North America are concerned about governments' more aggressive pursuit of foreign companies' profits, taxes on passive income, and taxes on repatriated earnings.

Perhaps not surprisingly, CFOs reveal a continuing focus on protecting earnings and managing risk. Over the past five years, CFOs say their companies have taken extensive steps to improve risk awareness, clarify responsibility, and plan for risk events. The dominant focus has been on operational risk, but CFOs say they have also gotten much more aggressive about financial risks in general and about de-risking their retirement liabilities in particular.

Aligned CFO compensation

On top of their executive obligation to pursue growth and profitability, CFOs have another strong motivator – their compensation. Nearly two-thirds of CFOs say growth has a moderate or strong impact on their pay – and that's just through direct growth metrics that don't account for the impact of growth on other metrics like share prices.

Growth is important, but profitability is still king when it comes to driving CFO compensation. More than 95% of CFOs report at least moderate influence and 75% report strong influence. But it is interesting to note that economic performance (through metrics like ROIC that incorporate both income statement and balance sheet measures) are the next strongest driver of CFO pay, with more than 70% of CFOs reporting moderate or strong influence. Also interesting is that measures more limited to the functional scope of finance (factors like liquidity, cost of capital, treasury returns, and tax efficiency) are considerably less influential – but there are important industry differences.

CFOs' incentives also appear increasingly aligned with shareholder returns. Nearly 70% of CFOs from public companies cite moderate to strong pay impacts from share prices, and nearly two-thirds say earnings-per-share (EPS) has a moderate to strong influence. (Note that some stakeholders have recently argued that tying executive pay to EPS produces an incentive to buy back shares, and this quarter's findings suggest a substantial number of CFOs might be in this position.)

Overall, CFOs' compensation appears to be increasingly aligned with that of CEOs – and reflective of their expanding roles, authority, and influence.

What's next?

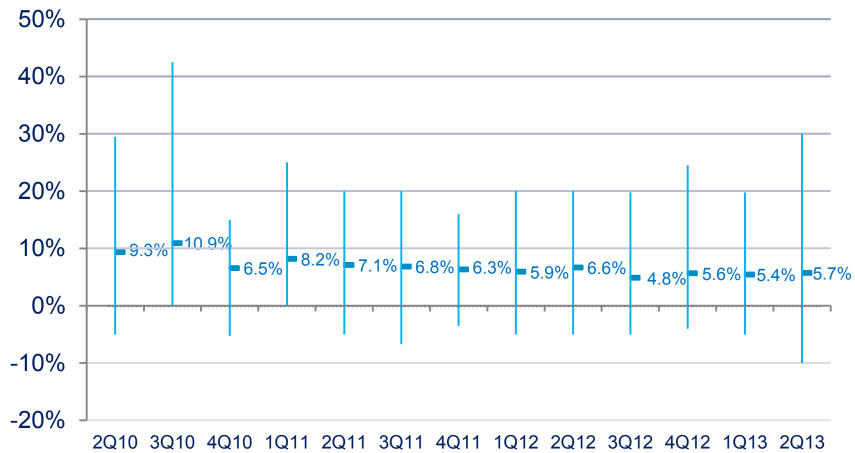
Clearly, the surging optimism visible in this quarter's survey is welcome news. But looking forward, it is hard not to wonder if future sales, earnings, hiring, and investment will catch up with the optimism or if the optimism will fall back in line with CFOs' still-muted growth expectations.

CFOs' palpable optimism this quarter around the future of North American economies suggests CFOs think the former is more likely than the latter, and unusually high variability in CFOs' growth expectations suggests we may indeed be at a transition point. Let's hope the transition will be a return to normal growth and not just a return to volatility.

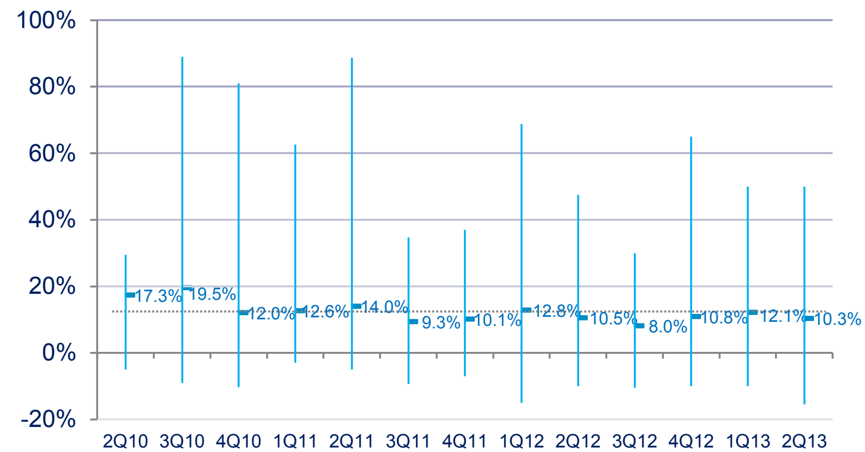
Growth Trends

CFOs' expected year-over-year increases in growth metrics

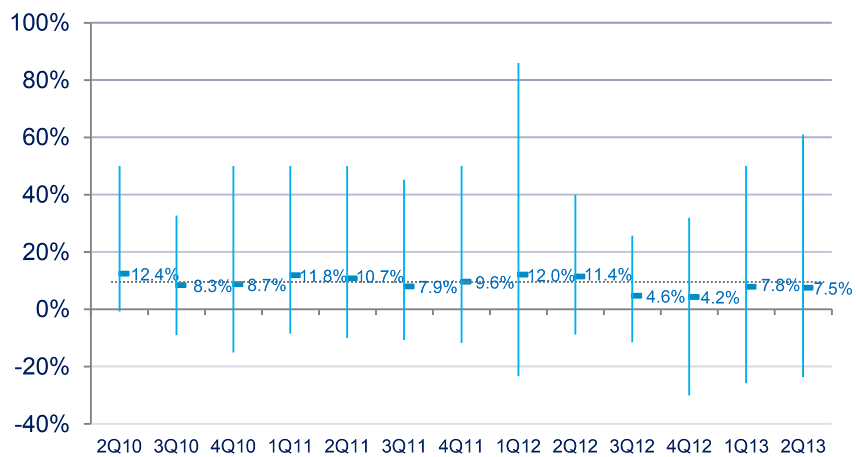
Sales Growth



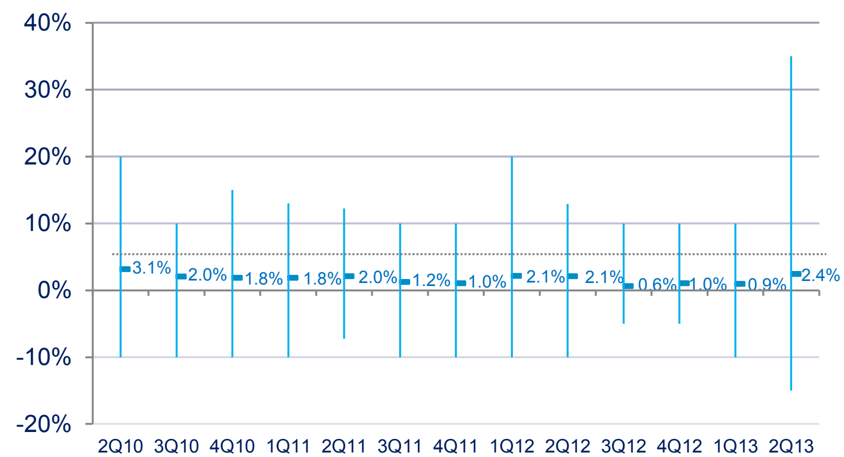
Earnings Growth



Capital Spending Growth



Domestic Employment Growth



Vertical lines indicate range for responses between 5th and 95th percentile.
Horizontal marks indicate outlier-adjusted means.
Dotted lines indicate 3-year average (simple mean)

Growth Trends

CFOs' Year-Over-Year Expectations

(Mean growth rate*, median growth rate, and percent of CFOs who expect gains)

	2Q10	3Q10	4Q10	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13
Sales	9.3%	10.9%	6.5%	8.2%	7.1%	6.8%	6.3%	5.9%	6.6%	4.8%	5.6%	5.4%	5.7%
	6.0%	10.0%	5.0%	5.0%	5.5%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
	84%	93%	81%	89%	80%	83%	87%	79%	85%	82%	83%	81%	84%
Earnings	17.3%	19.5%	12.0%	12.6%	14.0%	9.3%	10.1%	12.8%	10.5%	8.0%	10.9%	12.1%	10.3%
	6.0%	10.0%	8.0%	10.0%	10.0%	8.0%	9.0%	9.5%	8.5%	6.0%	7.0%	10.0%	10.0%
	89%	93%	80%	83%	83%	82%	84%	79%	81%	84%	76%	84%	83%
Dividends	6.5%	8.6%	4.1%	4.4%	3.7%	3.5%	2.4%	2.2%	3.9%	2.5%	2.5%	3.6%	4.5%
	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
	38%	39%	28%	36%	35%	41%	27%	31%	33%	30%	29%	38%	40%
Capital spending	12.4%	8.3%	8.7%	11.8%	10.7%	7.9%	9.6%	12.0%	11.4%	4.6%	4.2%	7.8%	7.5%
	5.0%	5.0%	4.0%	5.0%	10.0%	5.0%	5.0%	6.0%	10.0%	3.0%	0.0%	0.0%	3.5%
	62%	58%	57%	61%	69%	59%	61%	68%	70%	53%	43%	57%	57%
Number of domestic personnel	3.1%	2.0%	1.8%	1.8%	2.0%	1.2%	1.0%	2.1%	2.1%	0.6%	1.0%	0.9%	2.4%
	0.5%	2.0%	1.0%	1.0%	2.0%	1.0%	1.0%	1.0%	1.0%	0.0%	0.0%	0.0%	0.0%
	50%	60%	48%	61%	64%	52%	51%	51%	52%	40%	40%	43%	46%
Number of offshore personnel	3.5%	2.8%	3.6%	3.7%	4.1%	2.9%	4.8%	3.7%	3.8%	1.5%	0.5%	2.4%	2.5%
	0.0%	0.0%	0.0%	0.0%	2.0%	0.0%	0.5%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
	41%	49%	47%	41%	57%	37%	50%	43%	41%	30%	32%	39%	36%
Use of offshore/outsourced third parties	2.9%	1.4%	2.8%	2.2%	2.2%	3.1%	3.7%	2.5%	3.6%	1.6%	2.3%	2.6%	2.3%
	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
	35%	37%	32%	41%	31%	36%	49%	26%	30%	28%	28%	35%	31%

*All means been adjusted to eliminate the effects of stark outliers.

Business Environment

Top aids and impediments to growth

Top aids and impediments to growth
Across the broader business environment, which factors do CFOs believe will most help or hinder their companies' growth?

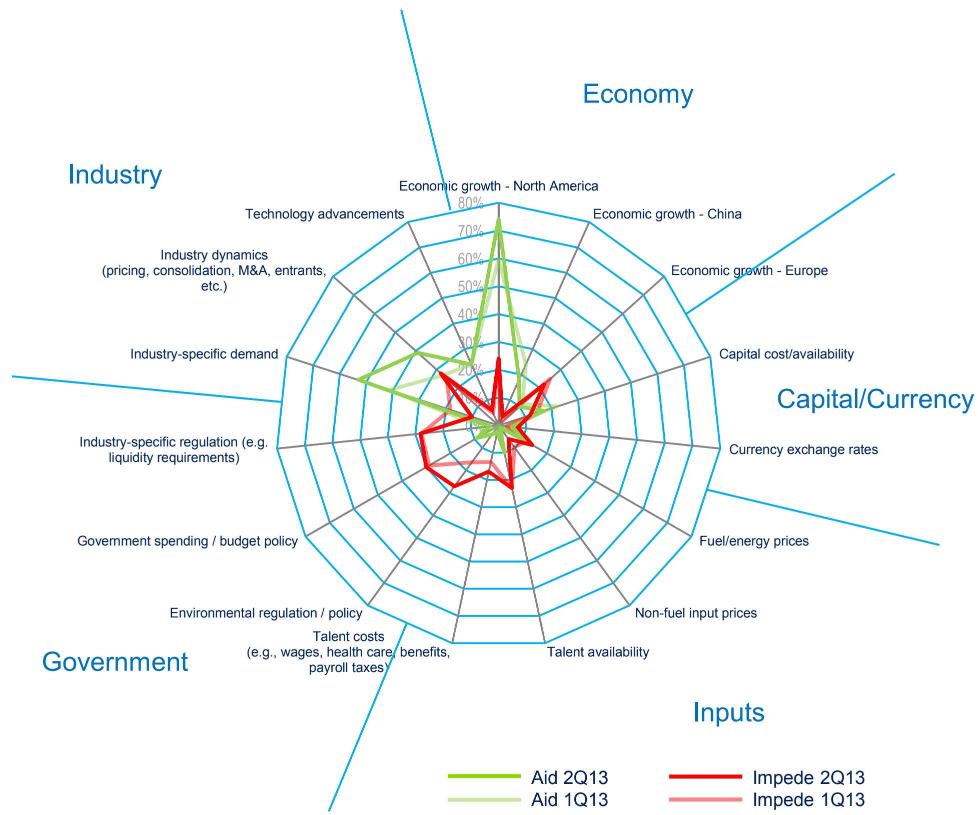
Even more than last quarter, the most positive factor in helping companies grow is the status of the North American economies:

- **The state of the North American economies** is the top growth aid, with more than 74% (60% last quarter) of CFOs naming it in their top three. This sentiment is fairly strong across all sectors except Healthcare/Pharma.
- **Industry-specific demand** is next at about 53% (40% last quarter), driven by particularly positive perceptions in the Retail/Wholesale sector.
- **Industry dynamics** are a positive factor for 39**%** of CFOs overall (27% last quarter) and for more than 55% in Manufacturing and Energy/Resources.
- **Technology advancements** are a top aid for 24% (same as last quarter), driven mostly by Healthcare/Pharma and T/M/E.
- **The state of the Chinese economy** is a top aid for 18% (23% last quarter) and for nearly 45% in Technology; **Europe's economy** is behind at just 10%.
- **Capital cost/availability** is a top aid for 17% (23% last quarter) of CFOs overall. Effects are strongest for Financial Services CFOs at 33%.

Top impediments to growth center heavily on public policy, with increasing concerns about environmental regulation:

- **Government spending/budget policy** is again the top impediment, with nearly 30% of CFOs naming it in their top three. Effects are strongest in Healthcare/Pharma at 83%.
- **Industry-specific regulation** is next at 28% (same as last quarter), with Financial Services, Energy/Resources, and Healthcare/Pharma above 40%.
- **Environmental regulation** jumped from just 16% last quarter to 27% this quarter, led overwhelmingly by Energy/Resources at 82%.
- **The state of European economies** is a top impediment for more than 20%, highest in Manufacturing and Services. The Technology sector, which saw Europe as a top impediment last quarter, sees it as a top aide this quarter.
- **Industry dynamics** are a top impediment for 25% of CFOs overall, but for more than 58% in Retail/Wholesale and T/M/E.
- **The state of the North American economies** is viewed as a top impediment by 24% of CFOs, with Services the most pessimistic.
- **Talent availability** is a top impediment for 23% of CFOs overall, with the strongest effects in Technology and Financial Services.

External Factors' Influence on Company Performance
Percent of CFOs naming each factor in their top three growth aids/impediments



**Please see Appendix for industry-specific findings.*

Business Environment

Assessment of economies

How do CFOs regard the current and future health of some of the world's major economies?

CFOs are feeling reasonably good about North America and China, but expectations for Europe are dour:

North America:

- About 60% of CFOs say the status of the North American economies is mediocre, and just over 30% describe it as good.
- U.S. sentiment is slightly ahead of Canadian sentiment, and Mexican CFOs are biased slightly toward pessimism.
- All three countries are substantially bullish on the status of the economies a year from now.
- CFOs from companies who derive most of their revenues from North America are the most pessimistic, but the vast majority believe conditions will be better a year from now.

Europe:

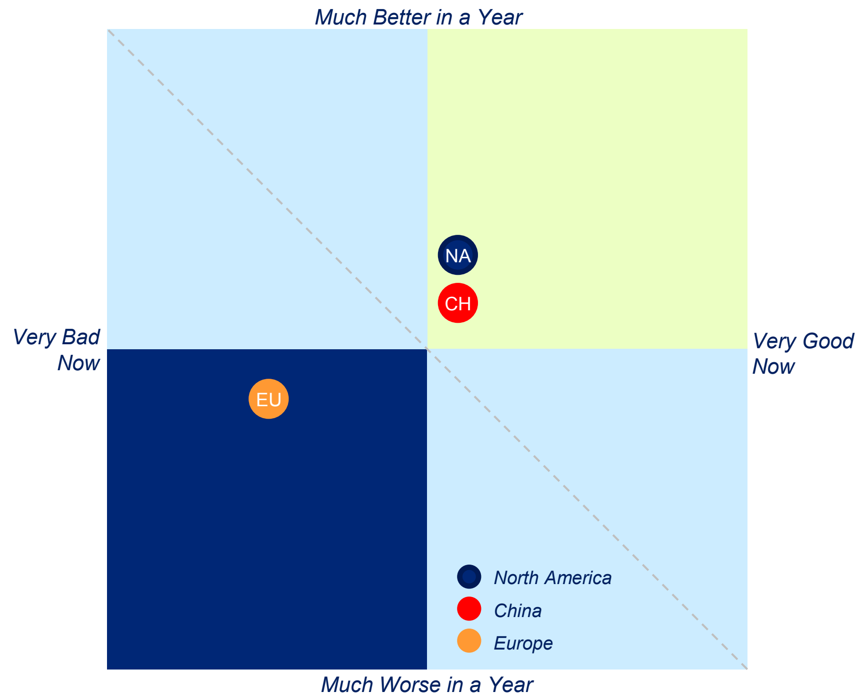
- About 90% of CFOs say the status of Europe's economy is bad, with only 1% describing it as good.
- Less than 15% of CFOs believe the economy will be better a year from now, and about 40% believe it will be worse.
- CFOs from companies who derive most of their revenues from outside North America are the most pessimistic about Europe's economy (in fact, nearly all describe its status as bad), and nearly all of these CFOs believe conditions will worsen over the next year.

China:

- Overall, about 35% of CFOs say China's economy is good, and just 15% regard it as bad.
- About 37% of CFOs believe the economy will be better a year from now, and about 10% believe it will be worse.

Status and Trajectory of Economies

CFOs' assessment of where economies currently stand and where they will be in a year



Region	Percent Optimistic*
North America	65%
Europe	14%
China	53%

* Refers to the percentage of respondents whose answer places them above and to the right of the dotted line in the top chart. Please see Appendix for industry-specific findings.

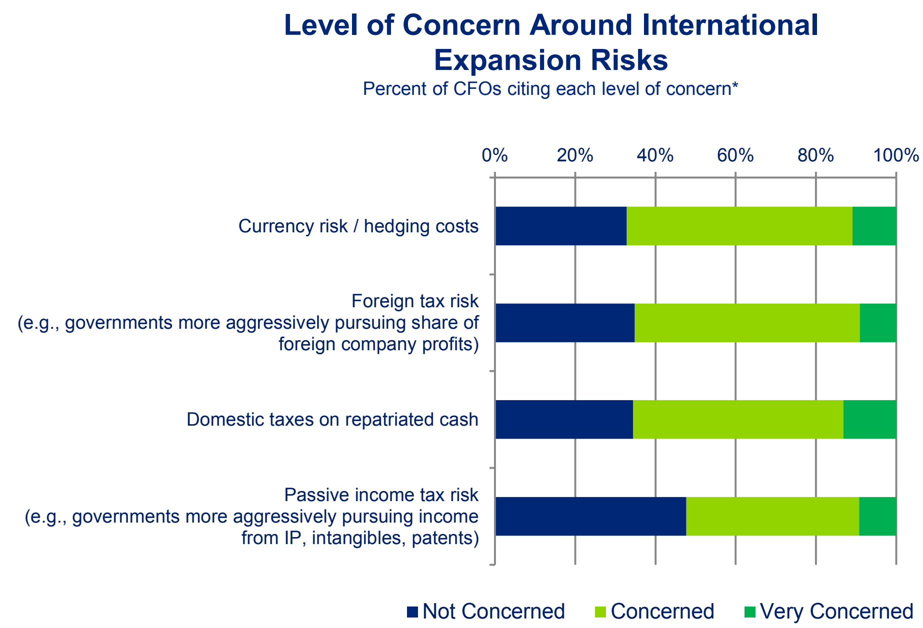
Business Environment

Risks to international growth

As companies plan for international growth, how concerned are they about some of the risks?

Companies planning for international growth are substantially concerned about currency risks and a variety of tax risks—especially within the Manufacturing sector:

- **Currency risk and hedging costs:** About two-thirds of CFOs are concerned about currency risks and the costs related to hedging. Just over 10% say they are very concerned, mostly driven by the Manufacturing sector.
- **Tax risk:** Two-thirds are concerned that foreign governments will step up efforts to tax the profits of companies from outside their borders (Manufacturing CFOs again voice the strongest concerns). The same proportion is concerned about the prospect of paying taxes on repatriated cash, and 13% are very concerned (nearly 90% of Manufacturing CFOs express concerns). The risk of governments more aggressively pursuing revenue from IP, intangibles, and patents is a concern for just over half of CFOs, with Manufacturing again expressing the strongest concerns.



* These results pertain only to the approximately 60% of CFOs who believed these risks were relevant for their company. Please see Appendix for industry-specific findings.

Business Environment

Assessment of equity valuations

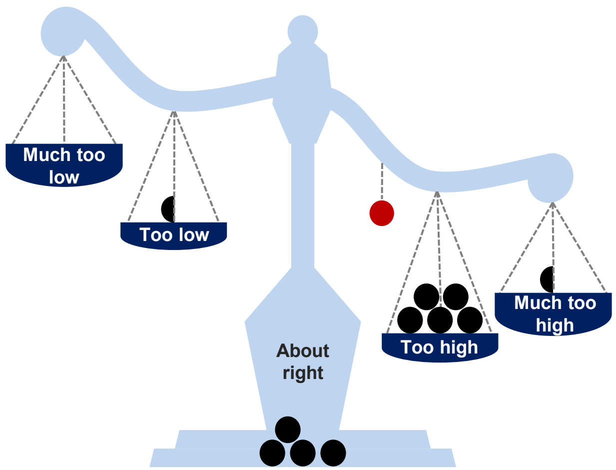
With U.S. equity markets up around 17% for the year, what do CFOs think about valuations?

CFOs believe equity valuations are too high—except when it comes to their own companies:

- Nearly 60% of CFOs think U.S. equities are overvalued, and only 4% think they are undervalued.
- About 39% of CFOs believe their company's stock is undervalued, and only 11% say it is overvalued. CFOs who believe their company is undervalued are mostly within Retail/Wholesale (45%), Energy/Resources (55%), and T/M/E (60%).

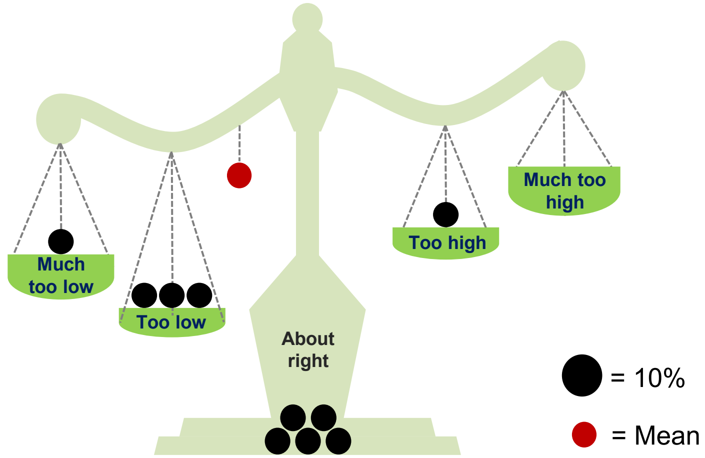
Equity Valuation

CFOs' assessment of their U.S. equities



Company stock valuation

CFOs' assessment of their company's stock



**Please see Appendix for industry-specific findings.*

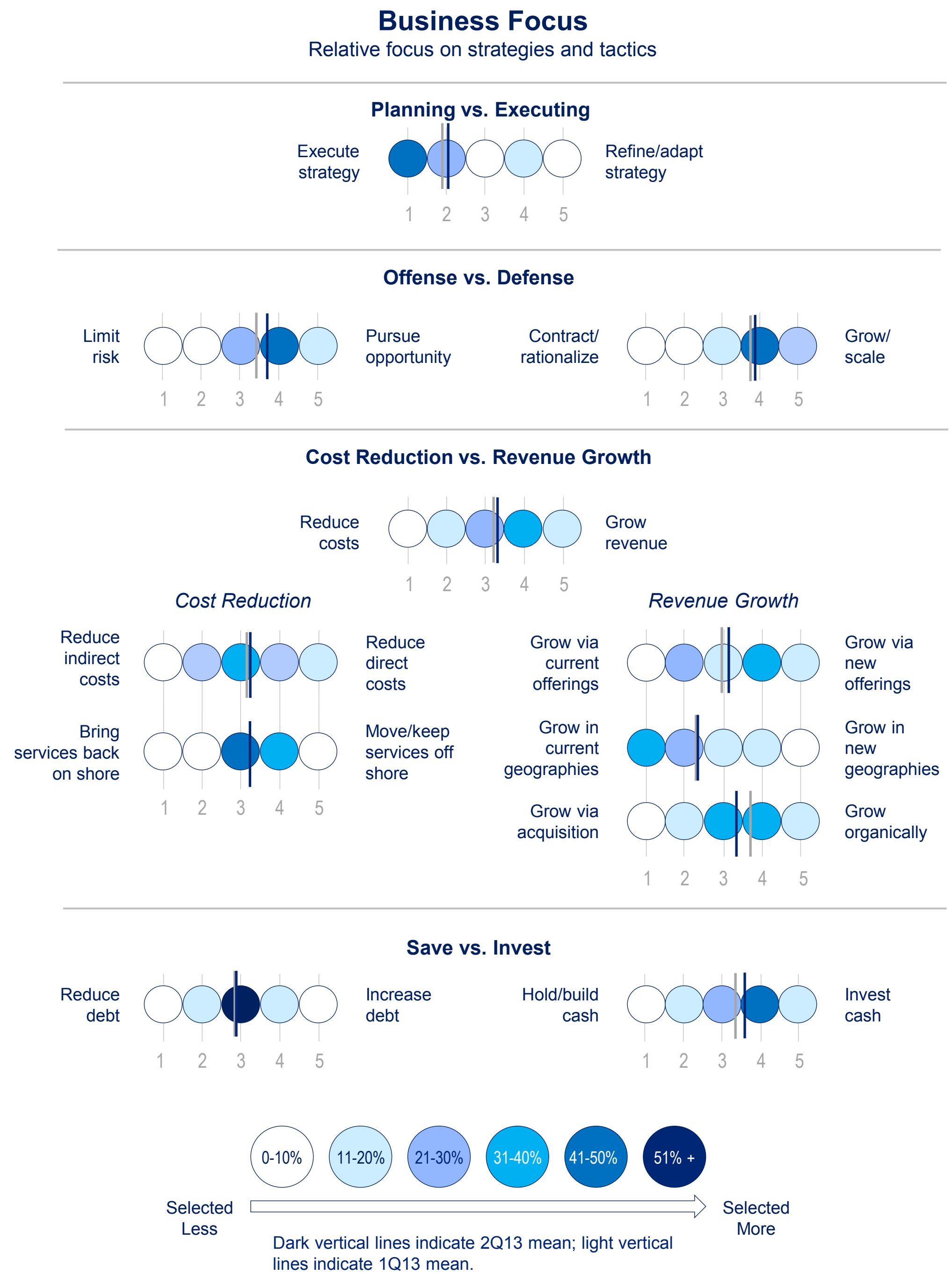
Company Priorities

Business focus

How are economic, political, and industry developments affecting companies' priorities?

Companies' rising focus on growth is evident in an increasing bias toward new offerings, new geographies, and rising capital investment:

- **Executing over planning**: Similar to last quarter, the bias across all sectors is toward executing strategy over refining/adapting it.
- **Offense over defense**: Companies mostly appear on the offensive, with "pursuing opportunity" ahead of "limiting risk," and "growing/scaling" ahead of "contracting/ rationalizing." These trends are quite consistent across all sectors.
- **Revenue over cost (widening)**: The bias is more toward revenue growth than it was last quarter. Energy/Resources is again the most cost-focused by a wide margin, and Technology, Healthcare/Pharma, and Services are the most revenue-focused.
- **New offerings over current offerings (substantial shift)**: Since last quarter, the bias has shifted toward new offerings, led by Technology and Healthcare/Pharma. Services and T/M/E.
- **Current geographies over new geographies**: The bias is still substantially toward current geographies—likely driven by both heavy reliance on the North American markets and this region's comparative economic health. Only Healthcare/Pharma is notably biased toward new geographies.
- **Organic growth over inorganic growth (narrowing)**: The bias is still toward organic growth, but Healthcare/Pharma leans substantially toward M&A.
- **Direct cost reduction over indirect cost reduction (narrowly)**: Retail/Wholesale and Services lean toward direct cost reduction, and Manufacturing shows the only bias toward indirect costs.
- **Off-shore over on-shore**: Companies are mostly inclined to move or keep services off shore, but 13% favor bringing services back to North America (led mostly by Services and Energy/Resources).
- **Investing over saving**: Cash still appears to be in sufficient supply with companies biased slightly toward reducing debt over increasing it, and substantially toward investing cash over holding/building it. There is substantial variability by industry.



Company Priorities

Plans for cash

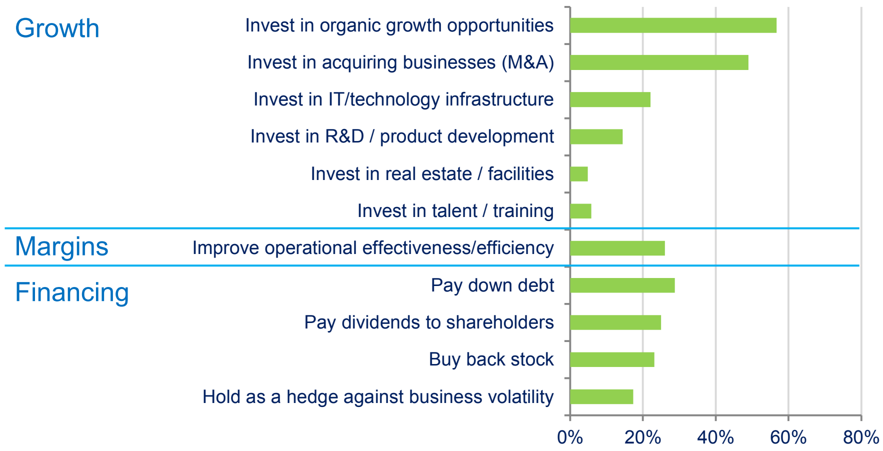
What do companies plan to do with their cash over the next year?

Growth is the highly-dominant cash use, with relatively little focus on further efficiency gains and financial risk mitigation:

- **Growth:** Growth is a top use of cash for three-quarters of all companies, with organic growth ahead of inorganic growth (Financial Services is well above the average for organic growth). A low focus on talent, real estate, and facilities investments seems to indicate reservations about spending in advance of growth-related investments paying off. R&D is a relatively low cash focus except in the Technology sector.
- **Margins**: Operational improvement is a relatively low focus except in the Financial Services and Services sectors.
- **Financing:** Financing-related uses of cash are prevalent, with 62% of CFOs citing some combination of paying down debt, buying back stock, or paying dividends. About one-third of publicly-traded companies say paying dividends will be a top cash use, and the same proportion say the same for buying back stock. About 15% say both are a priority. Less than 20% of all companies are focused on holding cash as a risk hedge, but more than 40% of companies in Healthcare/Pharma and Services cite this focus.

How Companies Will Use Cash in 2013

Percent of CFOs naming each risk a top-three cash use



**Please see Appendix for industry-specific findings.*

Company Priorities

Board concerns around risks

Which external and internal risks are top of mind for boards?

External Risks:

Boards' chief concerns are around economic health in North America and Europe, the effects of slow growth on competition, and governments' regulatory activity:

- **Economies**: Heavy reliance on consumer demand in North America makes this region's economy a top risk focus. But Europe's position as a top global importer makes its economic health a highly-monitored risk as well (especially for Technology firms). Only Retail/Wholesale is particularly focused on China.
- **Industry**: With slow growth driving heightened competition, boards are concerned about the impacts on volume, prices, and margins (especially true in Manufacturing, Technology, and T/M/E). Technology is substantially concerned about disruptive innovation, and Energy/Resources is very concerned about input prices.
- **Policy**: CFOs say boards are concerned about additional regulation that might make business conditions even tougher—particularly within Energy/Resources and Financial Services. Tax policy changes are a substantial concern for Retail/Wholesale, and fiscal policy changes are a concern for Financial Services and Manufacturing.
- **Capital**: Capital and equity market concerns are relatively low, but shareholder activism is a substantial concern in Energy/Resources and T/M/E. Financial Services boards are the only ones concerned about interest rates and equity markets.

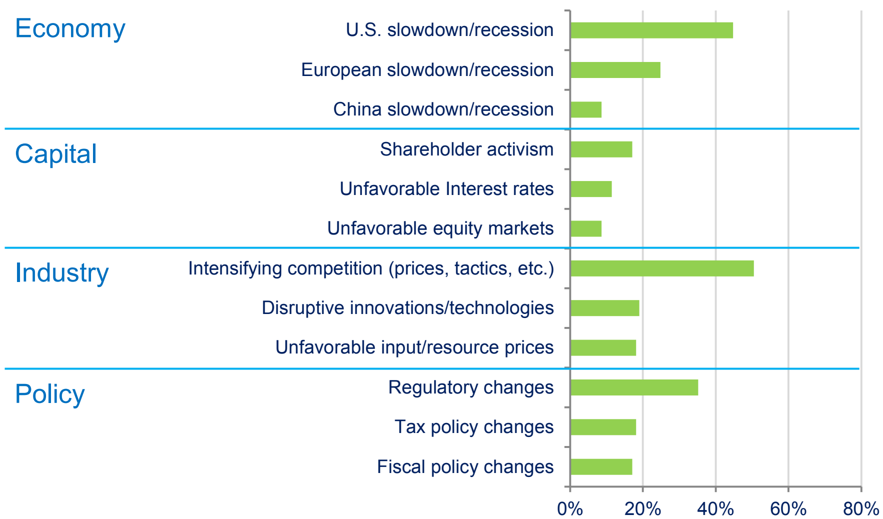
Internal Risks:

Boards are less worried about the quality of strategy than they are about having strategy reflected in investments and operations:

- **Strategic direction:** About 30% of CFOs say their boards are worried about strategic risks, with Technology and Healthcare/Pharma boards substantially higher. About 35% of boards are worried about the selection and/or execution of the right initiatives, with Services boards the most concerned.
- **Operations**: More than 60% of boards are worried about poor execution of strategy, with Technology boards the highest (78%).
- **People**: CFOs indicate strong board concerns about the loss and/or succession of key managerial and other talent, especially in the Manufacturing and Retail/Wholesale sectors.

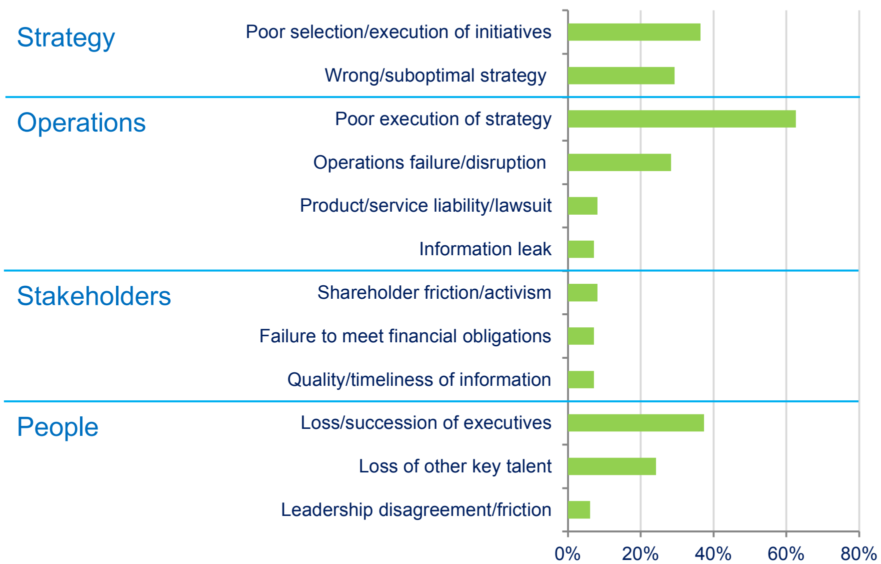
Board Worries – External

Percent of CFOs naming each risk a top-three concern



Board Worries – Internal

Percent of CFOs naming each risk a top-three concern



Company Priorities

Changes to risk management approaches

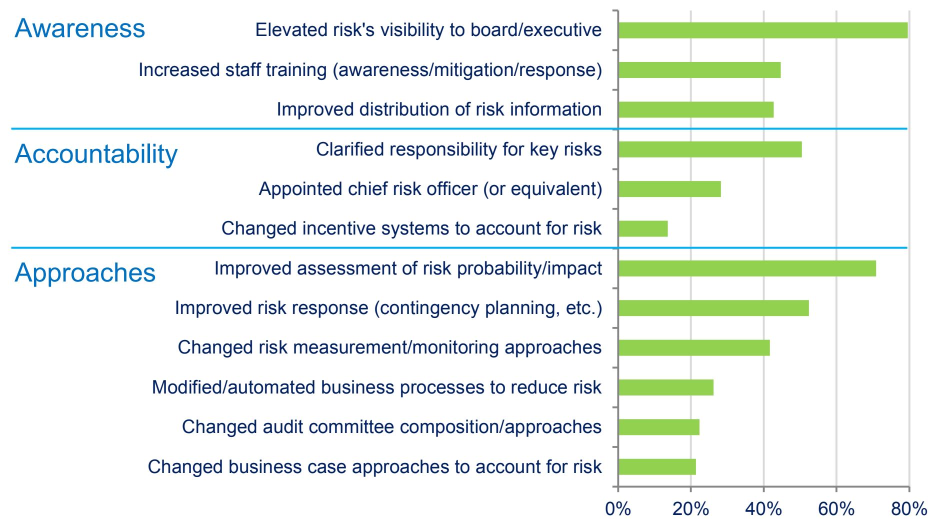
What have companies done to reinforce their risk management approaches over the past five years?

Companies have taken strong steps to improve risk awareness, clarify responsibility, and plan for risk events:

- **Awareness:** Nearly 80% of companies have raised the visibility of risk within their boards and executive teams, with all sectors except Technology over 60%. About 45% have increased staff training and/or improved the distribution of risk information.
- **Accountability:** Just over half have assigned or clarified responsibility for key risks, with Retail/Wholesale, Financial Services, and T/M/E the highest, and with Technology the lowest. Just under 30% of companies have assigned a Chief Risk Officer (or equivalent), but more than half of Financial Services and Healthcare/Pharma firms have done so. These two sectors are also the most likely to have substantially changed incentive systems to better account for risk.
- **Approaches:** More than 70% have improved their ability to assess the probability and impact of risks, with Technology again the only sector substantially lower. About 40% have changed their approach to measuring and monitoring risk, and more than 50% have improved their ability to respond to risk events (with Retail/Wholesale, Financial Services, and T/M/E the highest).

Changes to Risk Management Over the Past Five Years

Percent of CFOs citing each type of change



**Please see Appendix for industry-specific findings.*

Company Priorities

Retirement risk

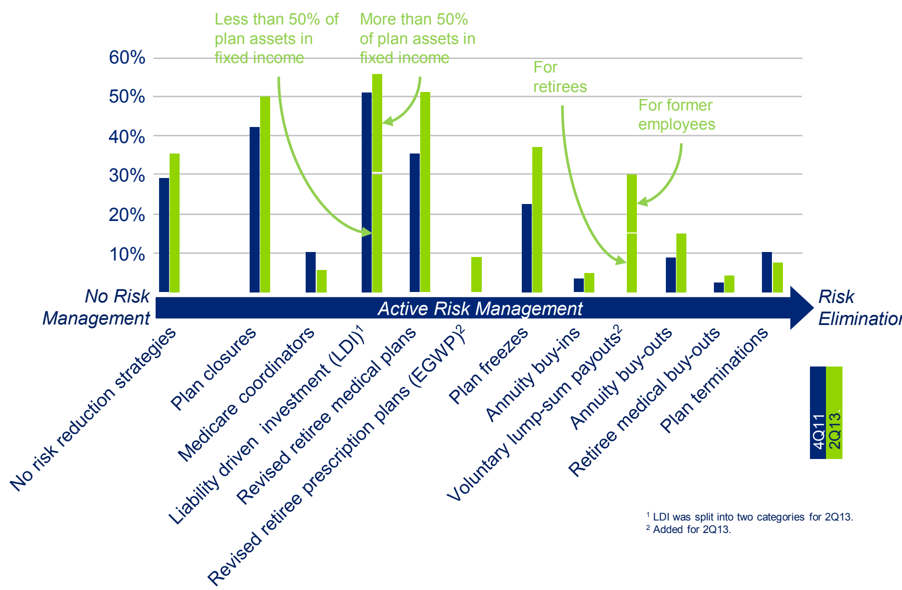
To what degree are companies managing their retirement risk, and how does this compare to 4Q11?

Since our 4Q11 survey, companies have gotten more aggressive about de-risking their retirement liabilities:

- **65% of respondents have tried at least one de-risking tactic** with substantial differences across industries. At the extremes are Manufacturing firms at 90% and Technology firms at just above 20% (likely due to a substantial difference in their respective use of retirement plans).
- **Companies that are reducing retirement risk appear to be employing a broader range of strategies**. From 4Q11 to 2Q13, the average number of risk-reducing strategies utilized rose from 2.0 to 2.7.
- **Liability-driven investment (LDI) is still the most-cited risk management strategy.** About 55% of CFOs indicate some degree of LDI use, and just under half of those are doing so with 50% or more of their plan assets.
- **Plan redesign approaches (focusing on minimizing liability growth and risk), already popular in 4Q11, have made further gains**. Plan closures were cited by 50% of risk-reducing respondents (up from 43%), complete plan freezes were reported by 37% (up from 23%), and revised retiree medical plans were cited by nearly 52% (up from 36%).
- **A growing proportion of companies have moved to the most aggressive end of the risk management continuum**. Aggressive approaches, such as plan terminations and retiree medical buy-outs remain relatively unpopular, but the attractiveness of eliminating (or greatly reducing) retirement risks has led to new use of voluntary lump-sum pay-outs (about 30%), increased use of plan freezes (37%), and a nearly doubled use of annuity buy-outs (about 15%).

Retirement Risk Reduction Strategies

Percent of respondents citing the use of each strategy
(among only CFOs who report using at least one strategy)



[1] LDI was split into two categories for 2Q13.
[2] Added for 2Q13.

Number of strategies employed	Proportion of respondents using risk reduction strategies
1	22%
2	32%
3	19%
4	15%
5	6%
6	6%

**Please see Appendix for industry-specific findings.*

Company Expectations

Sales and earnings

How is a slow-growth business environment affecting year-over-year sales and earnings expectations?

Sales:*

Sales growth expectations are similar to last quarter's—positive, but still below their long-term average:

- Sales are expected to rise 5.7% overall (similar to the levels we have seen over the last two quarters); the median is again 5%, with 84% of CFOs expecting year-over-year gains.
- Country-specific expectations are 5.5% for the U.S. (5.2% last quarter), 4.9% for Canada (7.4 % last quarter), and 8.3% for Mexico (6.6% last quarter).
- Technology expectations rose substantially and are now highest at about 10%; T/M/E is again lowest at just 2%.

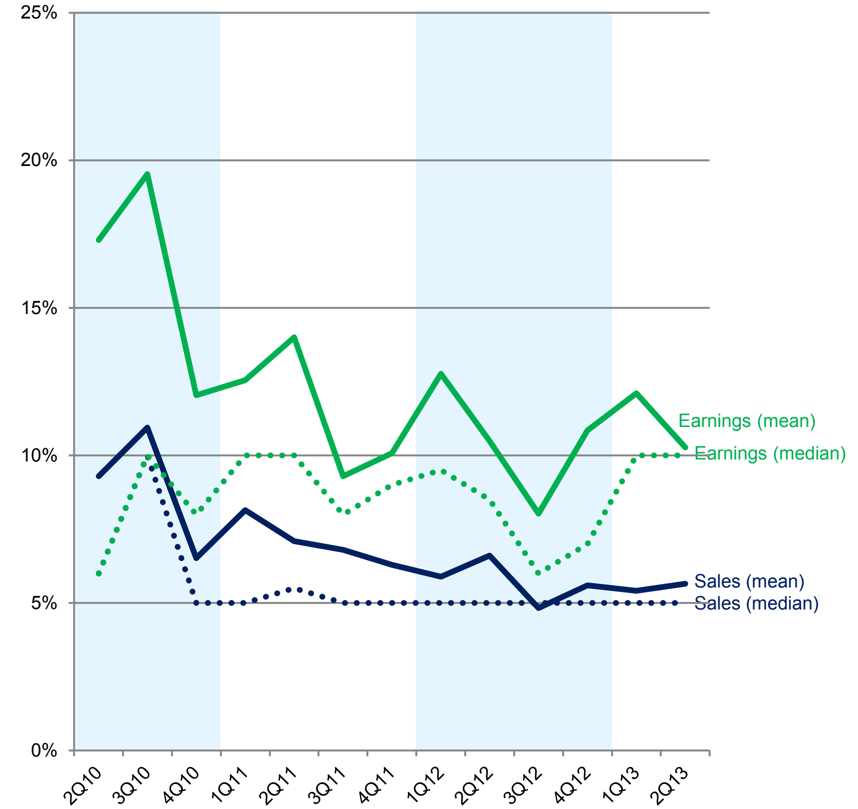
Earnings:*

Earnings growth expectations are still above their 3Q12 lows, but are below their long-term average:

- Earnings are expected to rise 10.3%, down a bit from the last two quarters, but well above the survey-low 8.0% in 3Q12; the median holds at 10%, and 83% of CFOs expect year-over-year gains.
- Country-specific expectations are 10.3% for the U.S. (12.0% last quarter), 8.0% for Canada (11.8 % last quarter), and 14.4% for Mexico (13.0% last quarter).
- Technology is highest at about 19%. Financial Services and T/M/E posted large declines in expectations, but Healthcare/Pharma is still lowest at just 1.2%.

Sales and Earnings*

Expected change year-over-year



**Averages have been adjusted to eliminate the effects of stark outliers. Please see Appendix for industry-specific findings.*

Company Expectations

Dividends and investment

How are companies using their cash in a slow-growth economic environment?

Dividends:*

Dividend growth expectations accelerated strongly and are at their highest level in nearly three years:

- Dividends are expected to rise 4.5%, well above their longer-term average. The median is still 0%, but 40% of CFOs now expect gains—the highest level we have seen in nearly two years.
- Country-specific expectations are 3.9% for the U.S. (4.0% last quarter), 1.5% for Canada (1.1% last quarter), and 14.6% for Mexico (2.0% last quarter, but note that the sample sizes have been relatively low).
- Manufacturing and Retail/Wholesale both posted notable gains and now sit above 8%. Energy/Resources and Services both expect declines.

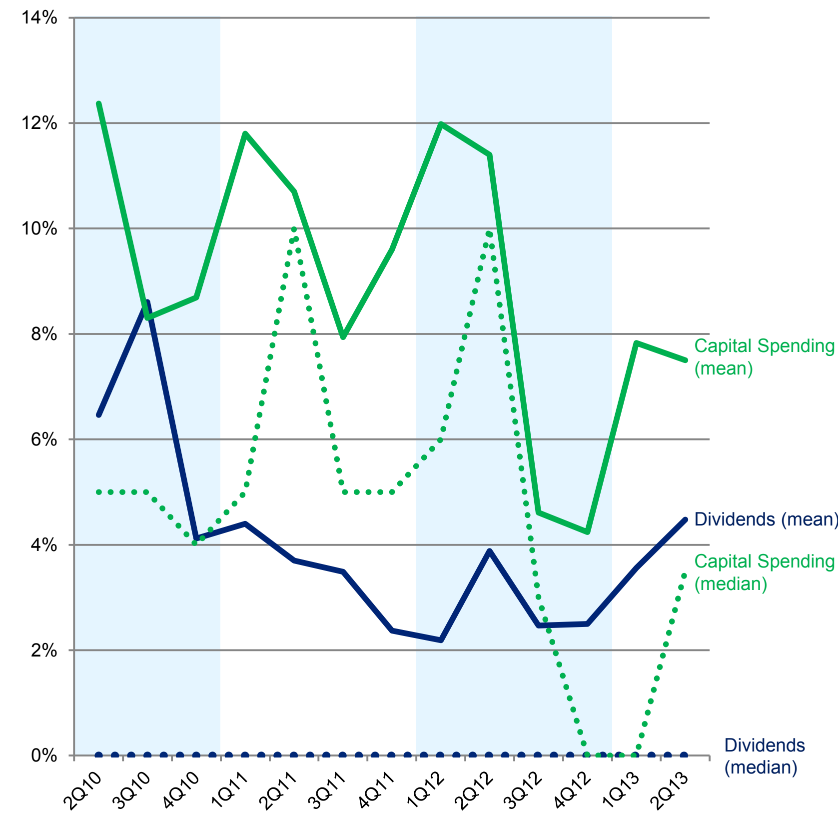
Capital investment:*

Capital spending growth expectations remained above their 3Q12 lows, but are still below their long-term average:

- Capital spending expectations declined slightly to 7.5%, but the median rose to 3.5%, and 57% of CFOs expect year-over-year gains.
- Country-specific expectations are 7.6% for the U.S. (10.9% last quarter), 5.5% for Canada (-9.4% last quarter), and 11.5% for Mexico (7.6% last quarter).
- Energy/Resources, T/M/E, and Services all posted substantial gains and now sit around 10%. Manufacturing fell sharply, and Healthcare Pharma fell again to -3.0%.

Investments*

Expected change year-over-year



**Averages have been adjusted to eliminate the effects of stark outliers. Please see Appendix for industry-specific findings.*

Company Expectations

Employment

Are companies confident enough in their growth prospects to increase hiring? And what will be the mix of domestic, offshore, and outsourced staffing growth?

Domestic hiring:*

Domestic hiring growth expectations improved in Canada and Mexico; U.S. expectations are still modest, and there is very high variability of expectations overall:

- Domestic hiring is expected to rise 2.4%—more than double the levels of recent quarters and the highest level we have seen in three years. The median is again 0%, but the variability of responses is much higher than in previous quarters. About 45% of CFOs expect year-over-year gains (comparatively high), and 21% expect cuts (comparatively low).
- Country-specific expectations are 1.3% for the U.S. (0.6% last quarter), 5.4% for Canada (3.5% last quarter), and 5.5% for Mexico (-1.0% last quarter).
- Technology, Financial Services, and Services all posted notable gains and sit above 4%; Energy/Resources and T/M/E both posted declines.

Offshore hiring and outsourcing:*

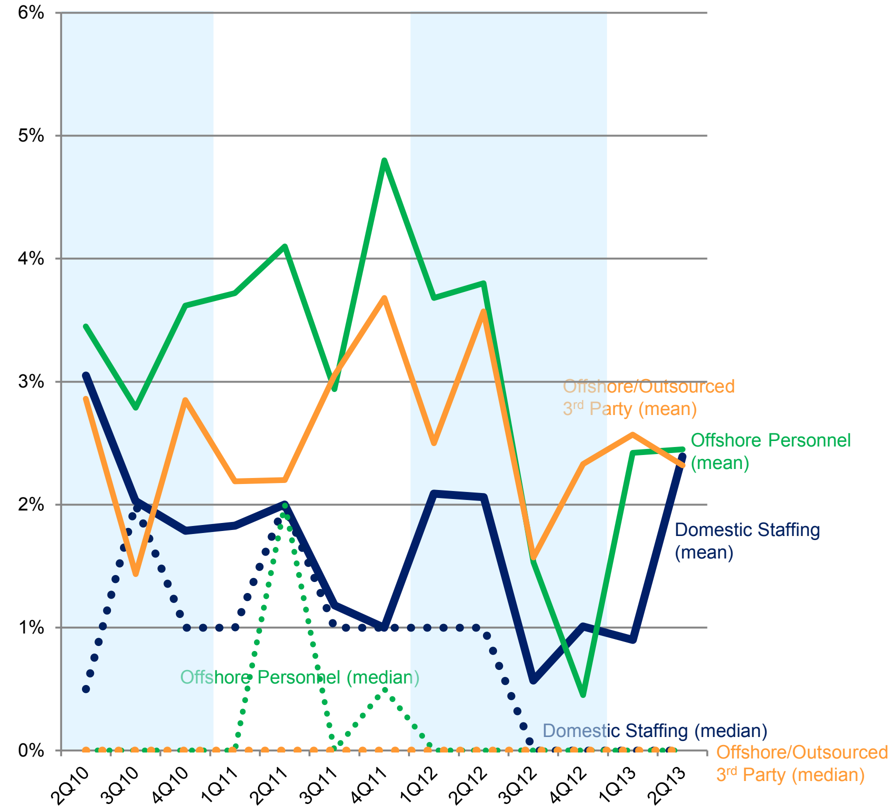
Offshore hiring growth expectations stayed above 4Q12's survey low; outsourcing is still rebounding, but only modestly:

- Offshore hiring held constant at 2.5%—still below the longer-term average of about 3%—with 36% of CFOs expecting year-over-year gains and just 5% expecting cuts. Technology is again highest at about 11%; Energy/Resources and Financial Services both turned from negative last quarter to positive this quarter.
- Outsourcing is expected to rise 2.3%, roughly consistent with the last two quarters. The median is again 0%, with 31% of CFOs expecting gains and just 3% expecting cuts. Technology, Financial Services, Healthcare/Pharma, and T/M/E are highest, similar to last quarter.

** Numbers with asterisks have been adjusted to eliminate the effects of stark outliers.*

Employment*

Expected change year-over-year



**Averages have been adjusted to eliminate the effects of stark outliers. Please see Appendix for industry-specific findings.*

Company Expectations

Own-company optimism

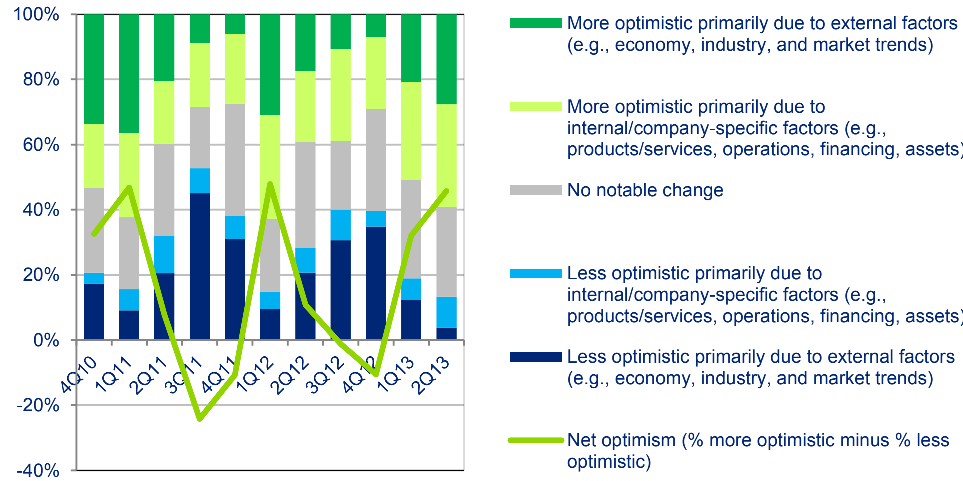
How do CFOs feel about their company's prospects compared to last quarter?

CFO optimism typically improves in the first quarter of the year, only to fall markedly in the second – but this year looks different:

- **U.S. equity markets strong:** Since the last survey, the S&P 500 has risen nearly 10%—a repeat of what happened between the 4Q12 and 1Q13 surveys.
- **Optimism still rising:** Net optimism rose markedly from -11 to +32 last quarter, and rose again to +46% this quarter. Nearly 60% of CFOs express rising optimism, and just under 15% express rising pessimism (a new survey low). The rising optimism is driven roughly equally by perceived improvements in internal company factors and in the external business environment.
- **All countries improving:** Optimism in the **U.S.** continues to rebound, with net optimism jumping from +33 last quarter to +46 this quarter. Net optimism in **Canada** rose modestly from -6 in 4Q12 to +7 last quarter. But this quarter it jumped to +39—overwhelmingly due to perceived improvements in internal company factors. Similar to previous quarters, about 60% of Mexican CFOs in **Mexico** report rising optimism, and none report a decline.
- **Strong industry differences:** Financial Services is again most optimistic (joined by Energy/Resources this quarter) and Manufacturing and Healthcare/Pharma comparatively less optimistic.

Own-Company Optimism

Net optimism and causes of rising/falling optimism



Please see Appendix for industry-specific findings.

Company Expectations

Most worrisome risks

Of all the internal and external factors that compete for CFOs' attention, which are most worrisome?

Over the past few quarters, worries have become less about specific events (e.g. recessions, collapses, and legislation) and more about longer-term lack of improvement:

- **Economic impact:** CFOs appear less worried about specific economies and more generally worried about worldwide economic recovery and growth. Financial Services cites the most concern about specific events, including inflation, equity market crashes, and interest rate shocks.
- **Government impact:** Especially in the U.S., CFOs express declining concern about the effects of government's taxing and spending policies on consumer demand, but more concern about the impacts of fiscal policy on longer-term economic health. Many continue to express concerns about potential new regulatory burdens, particularly within Financial Services. For the first time in several quarters, gridlock in Washington was not cited as a top concern.

Personal Priorities

Impact of metrics on CFO compensation

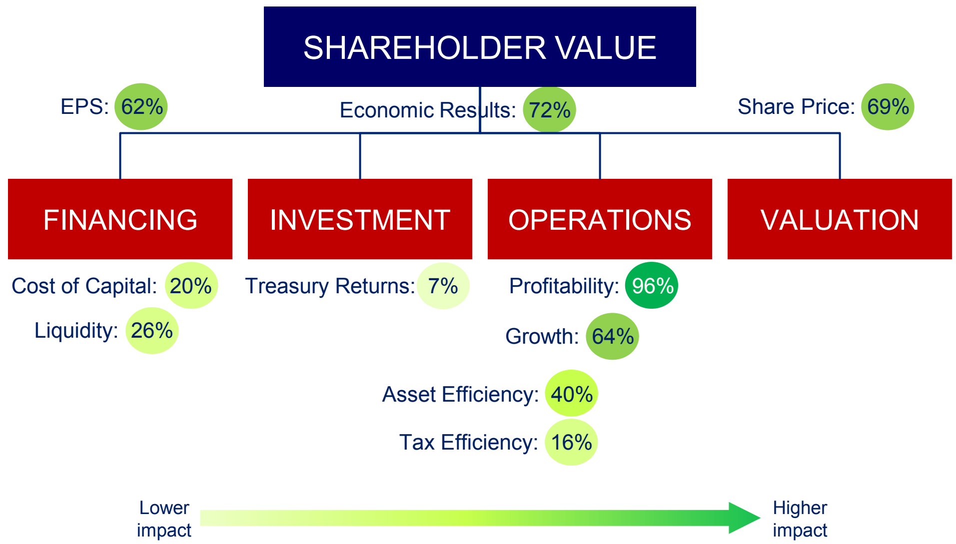
Which financial, investment, operational, and valuation measures have the strongest impact on CFO pay?

CFOs' salaries are impacted mostly by summary measures that reflect companies' income statement, balance sheet, and equity markets performance:

- **Profitability is still king.** Despite the notable impact of other measures, bottom line earnings are still the dominant driver of CFOs' incentive-based pay. About 95% report moderate to strong influence, with 75% reporting strong influence.
- **Both the "R" and the "I" in ROI matter.** Economic measures are the next strongest driver of CFO pay, with more than 70% of CFOs reporting moderate to strong influence (Retail/Wholesale and Technology are lower). **Asset efficiency** is one of the stronger operational metrics, with 40% reporting moderate to strong influence, led mostly by Manufacturing and Energy/Resources.
- **CFOs may have a pay-driven incentive to buy back shares.** Some shareholders and journalists have recently argued that, when a CFOs' pay is influenced by their companies' earnings per share (EPS), they have an incentive to pursue share buybacks. This quarter's survey findings suggest a substantial number of CFOs might be in this position, with nearly two-thirds of public company CFOs saying EPS has a moderate to strong influence on their pay—with little difference across industries.
- **CFOs' salaries are aligned with shareholders' returns.** With a significant proportion of their salaries tied to share price, CFOs have a vested interest in bolstering market valuations. Nearly 70% of public company CFOs cite moderate to strong influence from share prices, with Energy/Resources highest at 100% and Technology lowest at 29%.
- **Financing metrics have a relatively light impact on CFO pay.** Liquidity, cost of capital, and treasury returns are each cited by roughly half of CFOs as having at least some influence. There are exceptions, however, with Financial Services higher for liquidity and Energy/Resources higher for cost of capital.
- **Tax efficiency has a comparatively minor impact on CFO pay.** About 85% of CFOs cite no influence or only minor influence, but Manufacturing and Healthcare/Pharma cite stronger effects.

Impact of Performance on CFO Compensation

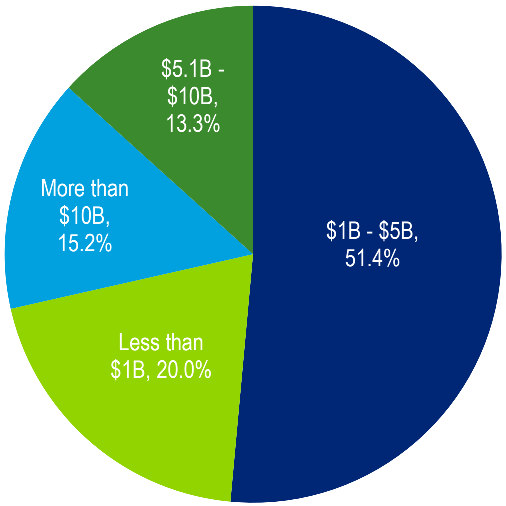
Percent of CFOs reporting moderate or high impact*



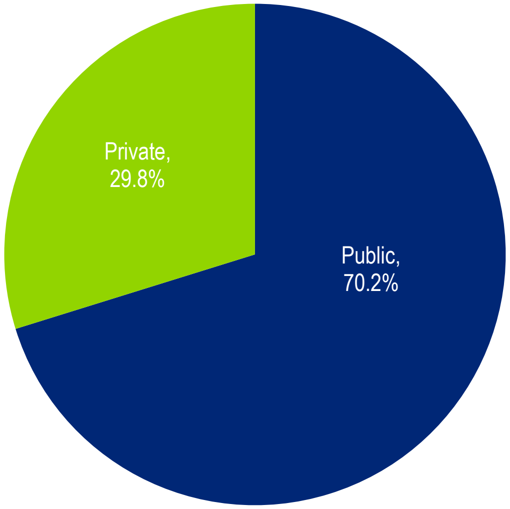
* Measures incorporating share numbers and share prices reflect responses only of CFOs from publicly-traded companies. Please see Appendix for industry-specific findings.

Demographics

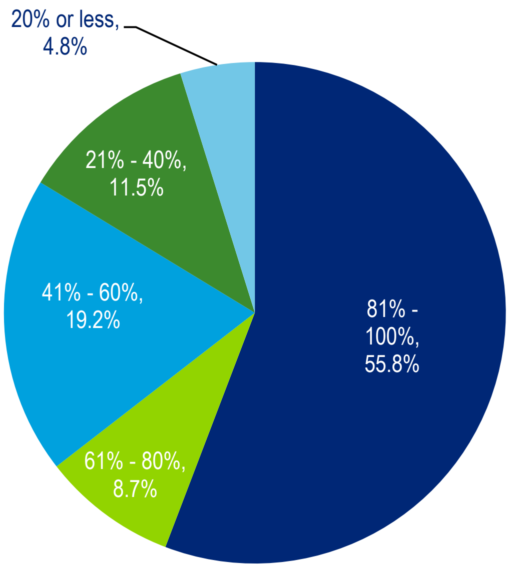
Annual Revenue ($U.S.)
(n=105)



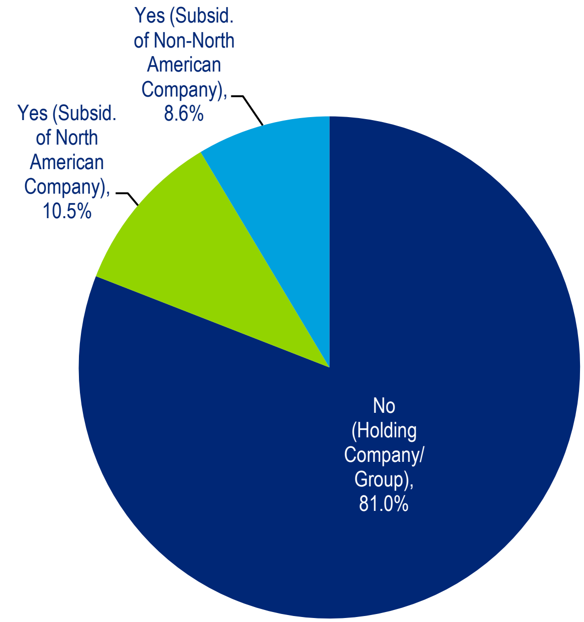
Ownership
(n=104)



Revenue from North America
(n=105)

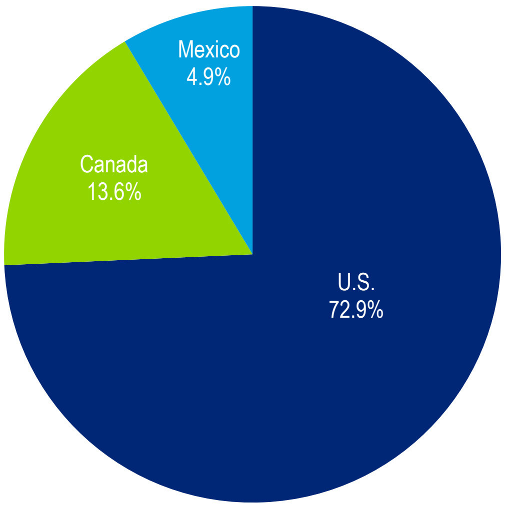


Subsidiary Company
(n=105)

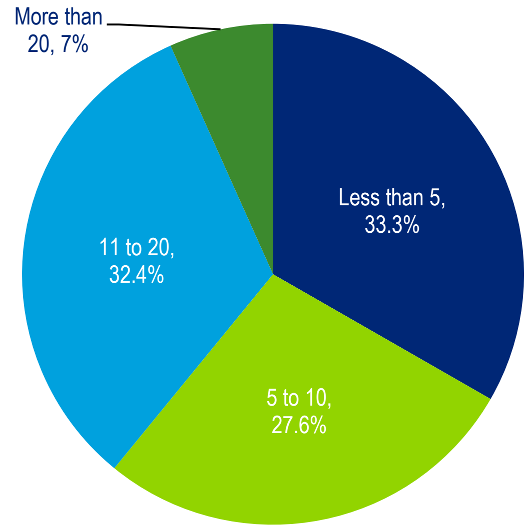


Demographics (cont.)

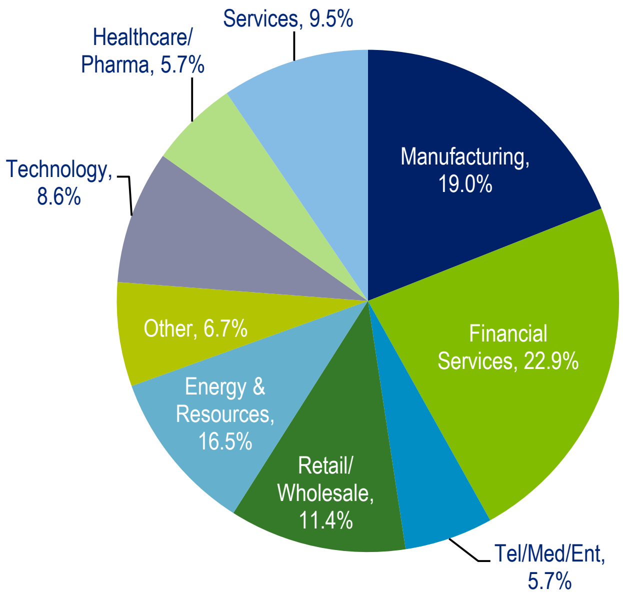
Country
(n=105)



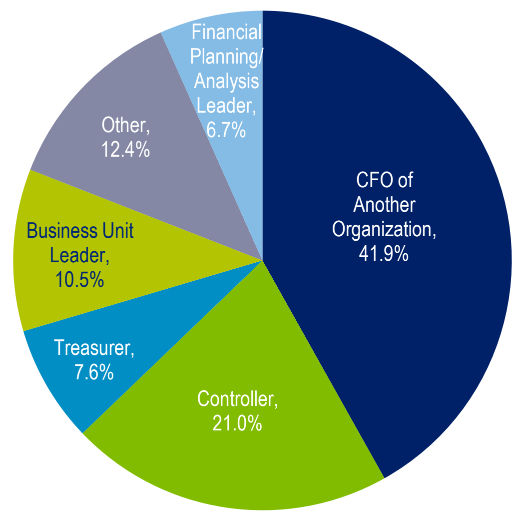
CFO Experience (Years)
(n=105)



Industry
(n=105)



Previous CFO Role
(n=105)



Methodology

Background

The Deloitte North American CFO Survey is a quarterly survey of CFOs from large, influential companies across North America. The purpose of the survey is to provide these CFOs with quarterly information regarding the perspectives and actions of their CFO peers across five areas: CFO career, finance organization, company, industry, and economy.

Participation

This survey seeks responses from client CFOs across the United States, Canada, and Mexico. The sample includes CFOs from public and private companies that are predominantly over $3B in annual revenue. Respondents are nearly exclusively CFOs. Participation is open to all sectors except for government.

Survey Execution

At the opening of each survey period, CFOs receive an email containing a link to an online survey hosted by a third-party service provider. The response period is typically two weeks, and CFOs receive a summary report approximately two weeks after the survey closes. Only CFOs who respond to the survey receive the summary report for the first two weeks after the report is released.

Nature of Results

This survey is a "pulse survey" intended to provide CFOs with information regarding their CFO peers' thinking across a variety of topics; it is not, nor is it intended to be, scientific in any way, including in its number of respondents, selection of respondents, or response rate – especially within individual industries. Accordingly, this report summarizes findings for the surveyed population but does not necessarily indicate economy- or industry-wide perceptions or trends.