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# Cautious optimism despite slowdown

## An economic evaluation by the Chief Financial Officers of large companies in Poland and Central Europe

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The opinions of representatives of many communities (including analysts, scientists, managers and lawyers) can result in the macro and micro-economic evaluation of a market situation. One of these groups comprises Chief Financial Officers (CFOs), whose forecasts contribute to a particularly reliable evaluation. They are not only directly responsible for the financial position and investment decisions of their companies, they also have direct contact with the market. Their practical experience, as well as their opinions (although these frequently differ from those of analysts) provides an additional perspective which allows better understanding of how the economic situation translates into company strategies.

# Introduction

I am delighted to present the results of the fourth Deloitte CE CFO Survey", which is carried out among the Chief Financial Officers (CFOs) of large companies in Central Europe. The report, which we publish on a regular basis, focuses on the expectations and challenges facing Polish CFOs. It also compares their sentiment with the attitude of CFOs from companies operating in 12 economies across Central Europe (Albania, Bulgaria, Croatia, the Czech Republic, Estonia, Latvia, Lithuania, Hungary, Romania, Serbia, Slovakia and Slovenia).

CFOs are one of the most reliable groups for influencing opinions about market conditions. Their opinions accurately reflect the economic situation, not only on a macro but also on a micro scale. Based on their opinions, it may be deduced that a slow return of positive attitudes and hopes for a period of new growth across our region of Europe is underway. However, not everybody shares this return of cautious optimism. The best attitudes are in the Baltic states and in Poland, where CFOs still anticipate moderate growth and an improving economic situation over the next12 months.
In Slovenia, the Czech Republic and Hungary, negative attitudes dominate, and the average for the region as a whole confirms strong concerns about a prolonged period of slowdown.

In many countries, companies are keen to continue strict cost and liquidity-control strategies as well as limiting their investments. However, in some countries including Poland, an appetite for risk is returning and strategies to increase sales from current and new markets are Yesing centre stage. This is a very positive signal, which announces the improving economic and market situation in these countries.

I hope that you find this report interesting and inspirational for the future. I would also like to invite you today to participate in the next edition of this survey, which will be carried out in October 2013.

**Krzysztof Pniewski**
Partner, leader of Deloitte CFO Programme in Poland
Deloitte Poland

# The most important trends observed in the CFO Survey in Poland – a significant but uncertain growth in optimism:

- Forecasts made by CFOs are reliable – to date they have accurately predicted changes in the economic situation in Poland
- After a six-month decline in the attitudes of Polish CFOs, there is a noticeable return of optimism among Polish enterprises – net optimism increased significantly from -28% to +24%.
- Economic slowdown in 2013 is a reality, although 50% of CFOs state that GDP growth may be as high as 1.5%. Inflation and EUR exchange rates will be stable (PLN 4.0-4.2). The level of economic uncertainty is very high. The highest risks in 2013 include recession and decreasing demand (over 48% of respondents). Expectations of increasing price pressure have grown significantly (from 13% to 22% of respondents). Expectations of pressure to increase costs have reduced (from 11% to 3%).
- Companies are responding to the 2013 slowdown with increased pressure to grow sales in their current markets (around 85% of respondents) and new markets (chosen by around 60%) as well as intensive actions to optimise direct costs (underYesen by around70%) and improve liquidity (by around 60% of respondents). CFOs expect no significant growth in unemployment during 2013.
- After a reduction in interest rates, appetite for risk, availability of loans and the attractiveness of share issues have all grown. However, investment still remains a low priority, and M&A activity is expected to remain largely unchanged in 2013.
- The most significant barriers to business operations include legal regulations regarding VAT (62%). Second place is Yesen by issues related to employment (the labour code – 36%, social security – 35%), which suggests an increased need for flexible employment during periods of economic uncertainty.
- Finance departments need to attract better employees, who can be true partners in business. Almost a third of companies are dissatisfied with its personnel in this area.

# The forecasts of Polish CFOs for 2013

## The fundamental challenges and concerns of Chief Financial Officers in Poland

Despite an intense slowdown of the economy, Polish CFOs are showing a significant increase in optimism. Its sources should be ascribed not only to external factors (such as better results in the eurozone, the pro-growth policy of the National Bank of Poland), but also to internal ones, including a sense of the strong financial and market position of their companies. In this context, restructuring and cost-reduction are no longer strategic priorities. More and more pressure is being placed on the search for new sources of revenues from existing markets (current domestic products and customers) as well as in new markets (new products, new customers and exports). The most significant threats anticipated by CFOs within the next 12 months are concerns regarding decreasing demand and growing pressure on prices.

# An evaluation of the economic situation

**The Baltic Tigers are confident about growth, with Poland just behind them**

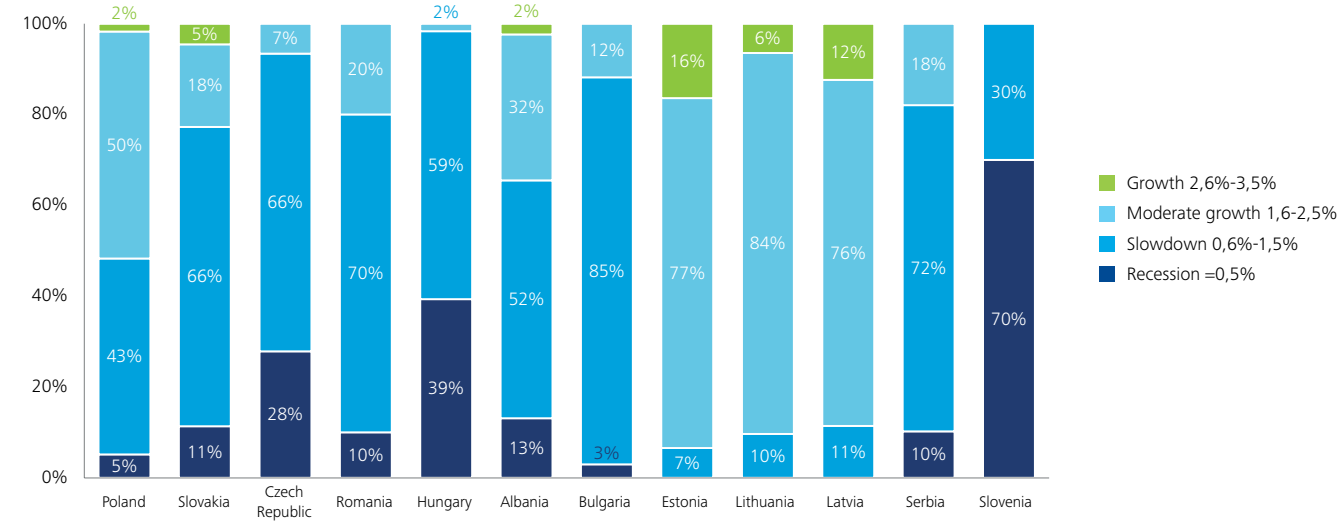
Expectations for economic growth in Poland in 2013 are moderately optimistic. Almost 95% of CFOs forecast economic growth, including more than half who estimate that it will be as high as 1.5%. This is a slight improvement in attitudes compared to the previous edition of the survey.

Although at the heart of Central Europe, Polish CFOs differ from most others due to their optimism – although those from the Baltic Tigers (Lithuania, Latvia and Estonia) are even more optimistic. However, it should be kept in mind that these countries experienced GDP decreases of around 15% in 2009, so today's growth forecasts of 1.5%-3% is comparatively insignificant.

Slovenians and Hungarians are at the other end of the scale. The former are experiencing a strong increase in uncertainty related to their domestic elections, the situation in Cyprus and, above all, the level of the country's indebtedness. The Hungarians, meanwhile, have long been trying to avoid the now imminent sanctions from the European Union for their failure to keep their budget deficit below 3% of GDP.

**Chart 1. GDP forecast**

What will GDP dynamics be in the opinion of CFOs?



## Moderate GDP growth, low inflation and a small increase in unemployment

Polish CFOs have slightly increased the optimism of their macro-economic forecasting:

- Now, 50% of them expect that GDP growth in 2013 will exceed 1.6% (as opposed to EIU forecasts of 1.4%)*.
- A significant decrease in expected inflation levels is also visible – almost 90% of CFOs estimate it will be lower than 3%, and a third predict a level even lower than official forecasts (2.1%)*.
- The majority of opinion still anticipates increased unemployment, but at a modest level (budget assumptions include a decrease from 14.4% in February to 13% at the end of year).
- A stable EUR/PLN exchange rate is forecast within the range of 4.00 to 4.19. This appears to indicate a slight expected appreciation for the PLN compared to the current exchange rate of 4.10 to 4.20.

**Chart 2. Forecast GDP change in 2013**

What will GDP dynamics be in the opinion of CFOs?

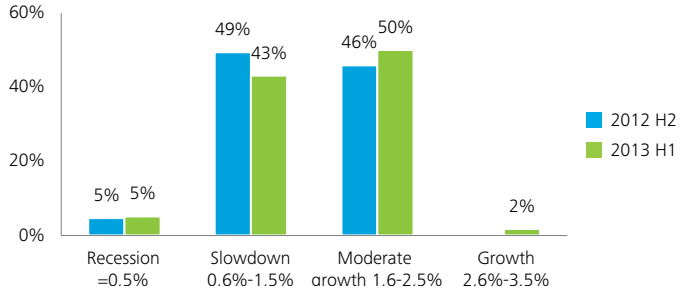



**Chart 3. Forecast unemployment within the next 12 months**

What will the unemployment rate be in opinion of CFOs?

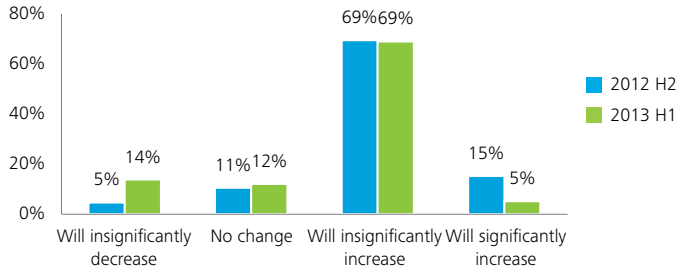



**Chart 4. Forecast inflation for 2013**

What will inflation be in opinion of CFOs?

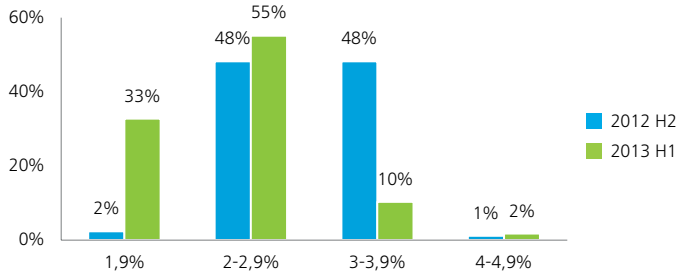
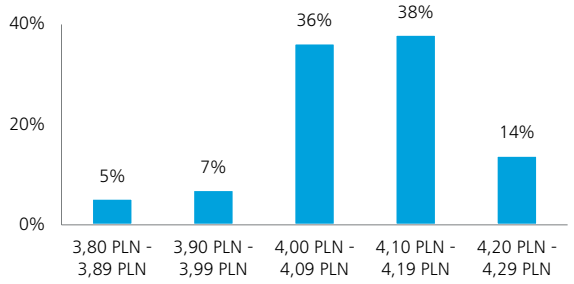



**Chart 5. Forecast exchange rate at the end of 2013**

What will exchange rate be in opinion of CFOs?




** Forecasts from the Economist Intelligence Unit (EIU)*

## Does the optimism of Polish CFOs extend to an improvement in GDP growth?

- The chart below shows the GDP forecasts made by the International Monetary Fund in 2013: world – 3.3%, developed economies – 1.2%, emerging economies – 5.3%, Poland – 1.3%.
- Forecasts made by CFOs for Poland also appear to be fairly consistent with those of the World Bank, although they are frequently more optimistic.
- It has been noticeable over time that there is correlation between the optimism of CFOs and increasing GDP in Poland.
- In the last six months, this optimism has significantly increased – can we Yese this as an indication of larger than forecast growth in GDP?

**Chart 6. GDP increase in the world**

GDP increases according to the IMF

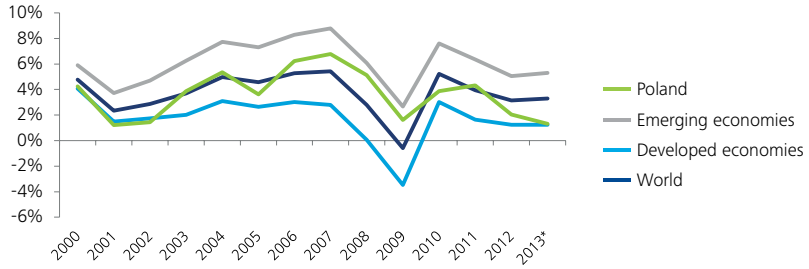
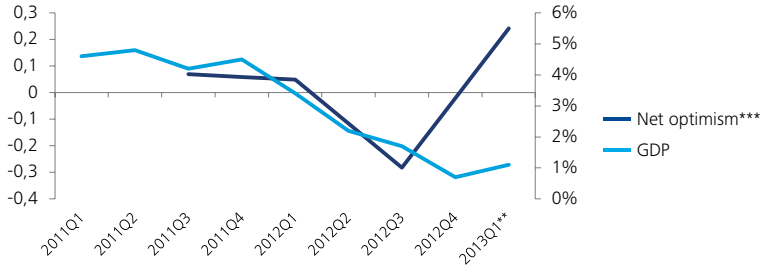



**Chart 7. CFOs optimism vs. GDP**

Do CFOs accurately estimate changes in GDP growth?




*Source: WEO, IMF*

** Forecast of IMF*

*** Forecast of INE PAN*

**** Data for even quarters are average of odd quarters*

## Better perspectives, but high uncertainty

Compared to six months ago, Polish CFOs have a more optimistic perception of their companies' financial outlook. Net optimism (which means the percentage of persons indicating improvement minus the percentage indicating a worsening situation) increased from -28 to +24. At the same time, there was further growth in CFOs' perception of uncertainty. This means they are being extremely cautious – on the one hand CFOs see an improving economic situation, but on the other they are aware that it is still very unstable.

**Chart 8. Economic uncertainty**

Evaluation of economic uncertainty by CFOs

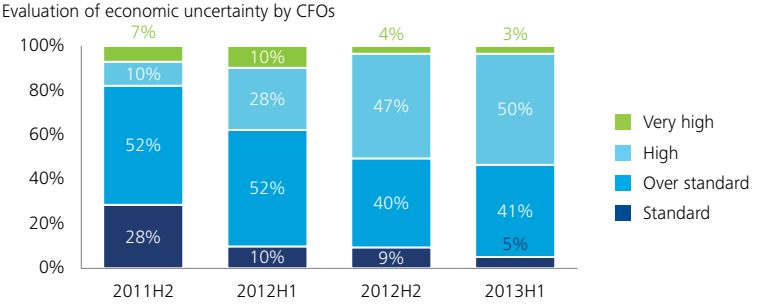
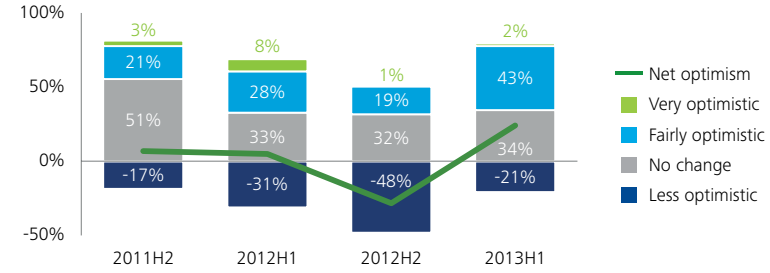



**Chart 9. Financial perspectives**

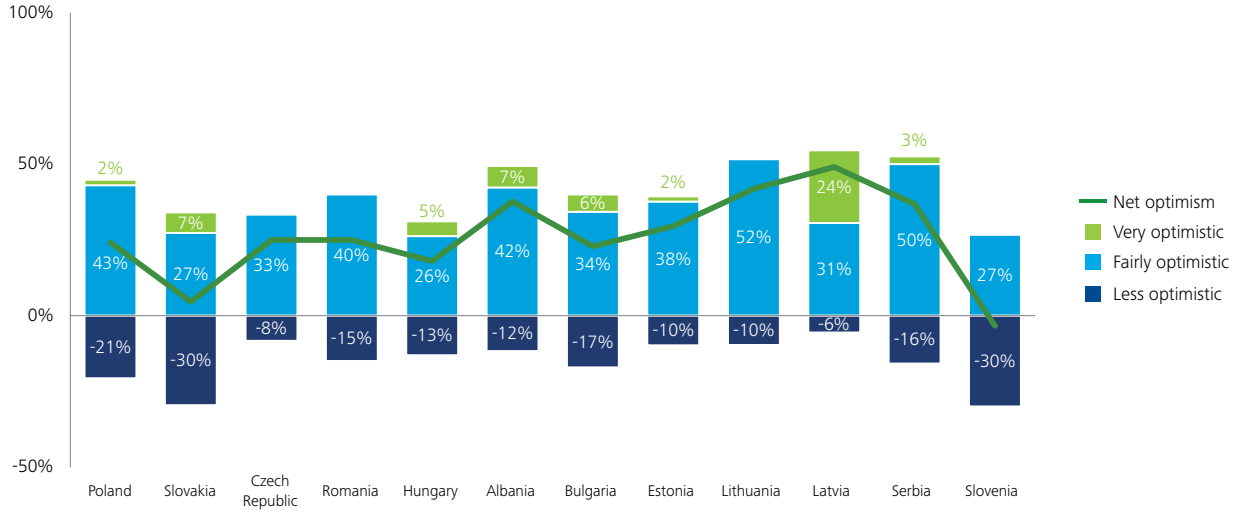
Financial perspectives comparing to situation 6 months ago



Despite such a significant increase in optimism, against the background of Central Europe Polish CFOs are mid-table. The greatest optimism level is to be seen in Lithuania and Latvia, which may be a result of the extreme slowdown that these countries have overcome. In Slovenia, which appears to have been hit by the final wave of the European crisis, CFOs arrived at a negative optimism index of -3%). It significantly influences evaluation of perspectives by CFOs in these areas.

**Chart 10. Financial perspectives**

Financial perspectives comparing to situation 6 months ago



# Key risks and business priorities

**Slowdown, decreasing demand and price pressures are the main threats**

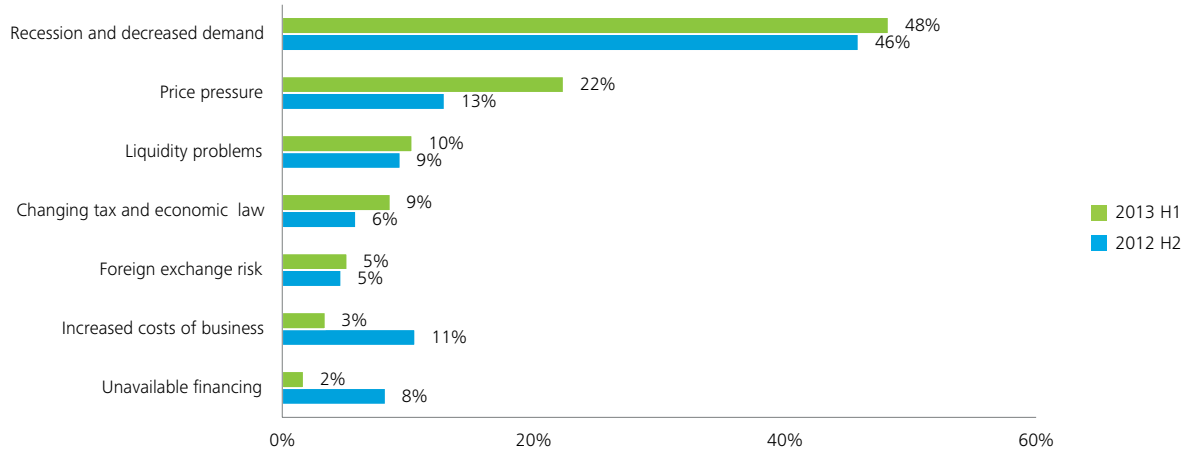
The most important areas that CFOs perceive as threats to their businesses are similar to those of September 2012. However there have also been some important changes. Slowdown and decreasing demand are still the main concerns (with 48% of respondents selecting this response).

Price pressures are directly connected with these issues, but significantly more CFOs highlighted them in this edition – 22% instead of 13%. This is probably caused by consistently falling inflation, which at the other end of the spectrum is also a source of CFO comfort as it reduces pressure to increase the costs of operations. Only 3% of CFOs that took part in the survey (compared to 11% in previous edition) indicated this factor as a significant risk. An additional confirmation of this statement is the significant decrease in the number of CFOs who are concerned about business financing – from 8% to 2%.

Based on such results, it may be concluded that the cycle of decreasing interest rates is primarily beneficial – it allows CFOs some "rest" from the search for liquidity and worries about costs, and lets them focus on developing the business and seeking new markets and new values to maintain existing prices and margins.

**Chart 11. Risk**

What risk factors do CFOs perceive as the most important?



# Enterprise strategies for 2013

### No change priorities – revenues high, investments low

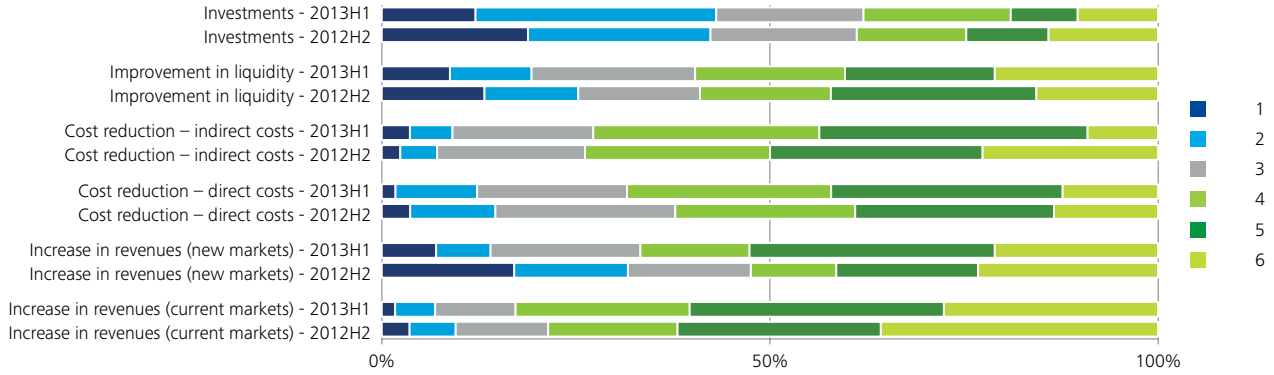
Unfortunately, despite the positive influence of extremely low interest rates, CFOs still do not see the necessity to invest. This is still the lowest of all evaluated priorities in the survey. However, this should not be surprising: in an environment of high economic uncertainty and significant concerns about demand, businesses do not see any value in new investments.

Their basic priorities still includes the battle to increase revenues from existing markets (although it should be considered whether maintaining an existing level actually is a battle at all). Moreover, there has been a significant increase in the importance of leveraging revenues from new markets, which is the most significant change since the previous edition. It therefore seems that CFOs are ready to underYese greater risks and enter new geographic areas to protect their businesses against slowdown.

**Chart 12. CFO priorities**

CFO priorities for the next 12 months

(1 - the lowest, 6 – the highest)

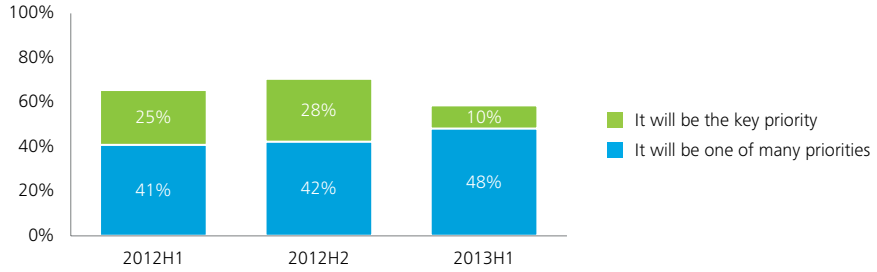


## Restructuring… already done?

The percentage of CFOs prioritising restructuring and changing the business model has significantly decreased (particularly those for whom it was a key task). However, the number of those for whom it is one of many priorities increased slightly. Such results may mean that some enterprises have already completed the restructuring process, meaning this issue has disappeared from their radars. Others are at such an advanced stage that they do not need to focus exclusively on this one issue to the exclusion of others which are similarly crucial or even more important.

**Chart 13. Restructuring as a priority**

To what extent will restructuring be a priority over the next year?



## Increased appetite for risk, but not in the form of investment

On the chart that shows risk appetite over the last 18 months, clear fluctuations are noticeable. This time, it is on the increase again. However, looking at the low priority that Polish CFOs give investment, this risk does not appear to include investment. Rather, they plan to increase their indebtedness on one hand (as indicated elsewhere in the survey), and on the other to conduct more aggressive development of their existing business, for example – by entering new markets.

It is slightly surprising that they place investments so far down their priorities compared to other countries. Only Slovenia, Albania and Romania place them lower. This may result from the high uncertainty that Polish CFOs expressed at the beginning of this survey. CFOs are more willing to invest even in other countries with worse forecasts, but that experience more stable conditions.

**Chart 14. CFO priorities**

To what extent are new investments a priority for the next 12 months

(1 - the lowest, 6 – the highest)

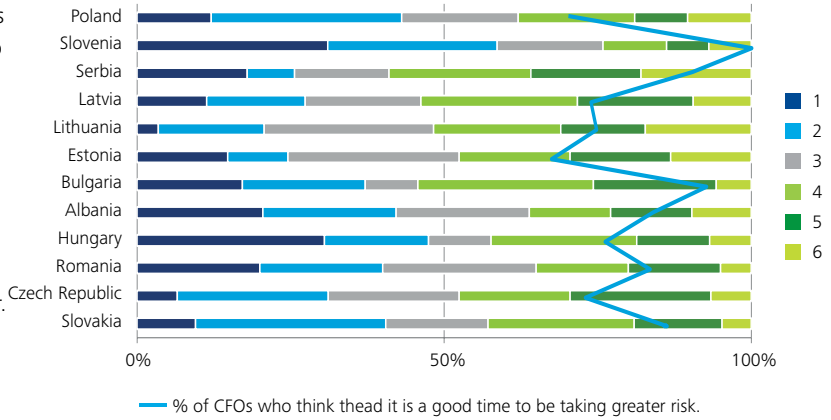
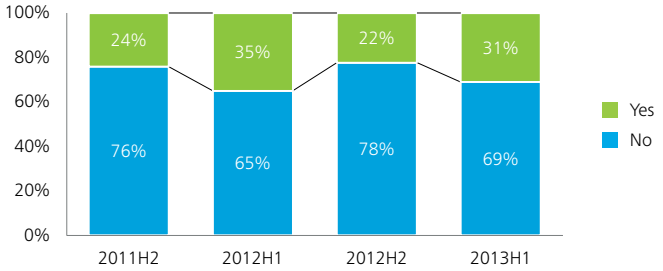



**Chart 15. Appetite for risk**

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



## Capital market becomes interesting again

Together with the return of stabilisation (and even gradual increases) to the Warsaw Stock Exchange, CFOs are more willing to hold share issues as a source of financing for their business operations.

This finding highlights that recovery is expected within the area of share issues (including the IPO market).

**Chart 16. Attractiveness of share issues**

How attractive are share issues as a source of financing?

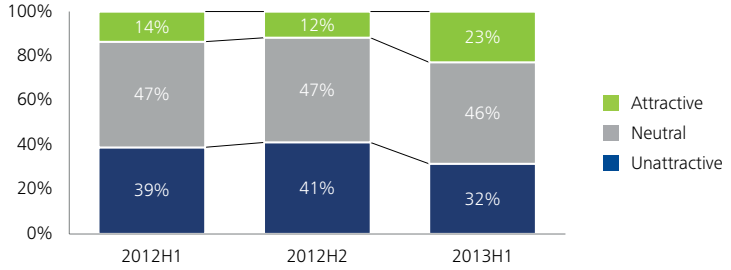
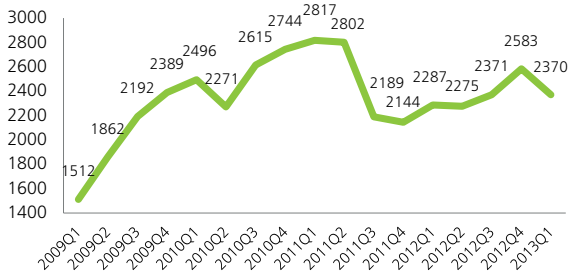



**Chart 17. WIG20**

Situation at stock exchange - WIG20 index




*Source: Warsaw Stock Exchange data – value of WIG20 index as of the last day of a given quarter*

## Higher availability of loans – a positive forecast for the banks

The loan as a source of financing has become slightly more attractive to Polish CFOs (although it should be said that based on the results it has actually becomes less unattractive).

However, evaluating the availability of loan finance is more significant. In a previous edition of this survey, CFOs noticed a significant worsening in the availability of loans. In the following six months this translated into the first decline since 2010 in the banking sector's receivables from enterprises (i.e. the total amount of the loans granted to business). It may therefore be concluded that in the next six months the upward trend, which started in the first quarter of last year, will be continued. It is the result of a significant improvement in credit availability in the opinion of CFOs.

**Chart 18. Attractiveness of loans**

How attractivene are loans as a source of financing?

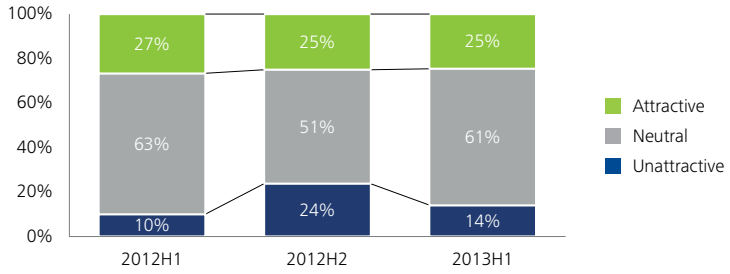
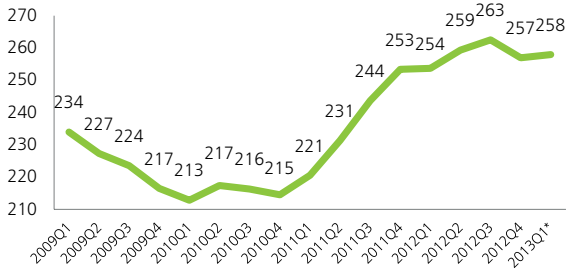



**Chart 19. Granted loans**

Size of bank receivables from enterprises

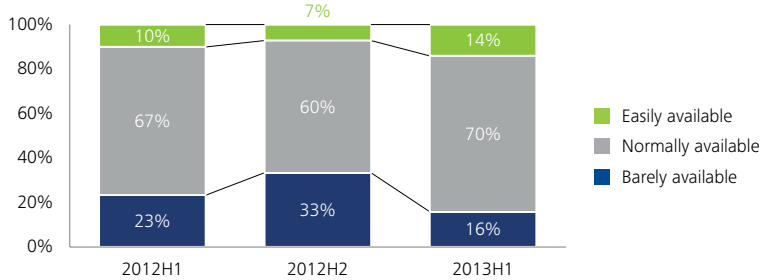



** Data for February 2013*

*Source: bank receivables from enterprises – NBP, 21.04.2013*

**Chart 20. Availability of loans**

How do CFOs evaluate the loan availability?



## Cheaper financing = higher indebtedness?

Polish CFOs are CE's most optimistic in terms of the decreasing costs of finance. 64% of them expect no growth in these costs, and 34% expect them to decrease. This may be interpreted in the context of an ongoing cycle of lowering interest rates. A natural consequence of such expectations might be an increase in indebtedness. The purpose behind the increased availability of cheap finance is after all to encourage companies to take loans.

A consequence of pessimistic CFO forecasts for the Slovenian economy (slowdown, no investments) also includes the forecast of significant increases in financing costs in this country.

**Chart 21. Planned level of indebtedness in Poland**

What is the planned level of indebtedness within 12 months

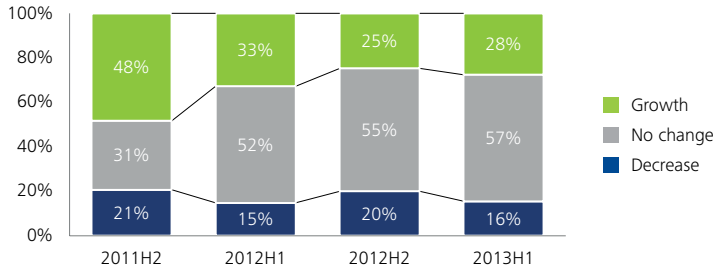



**Chart 22. Financing costs in Poland**

Forecast of changes in financing costs within 12 months

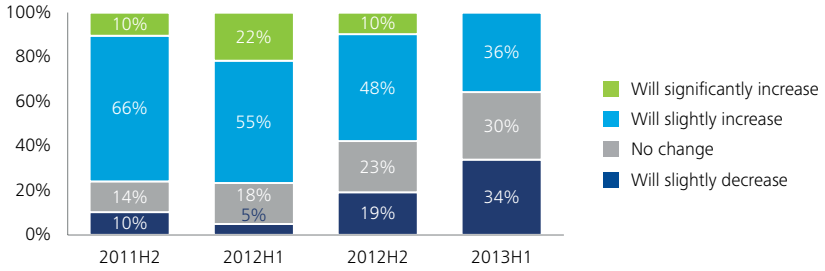
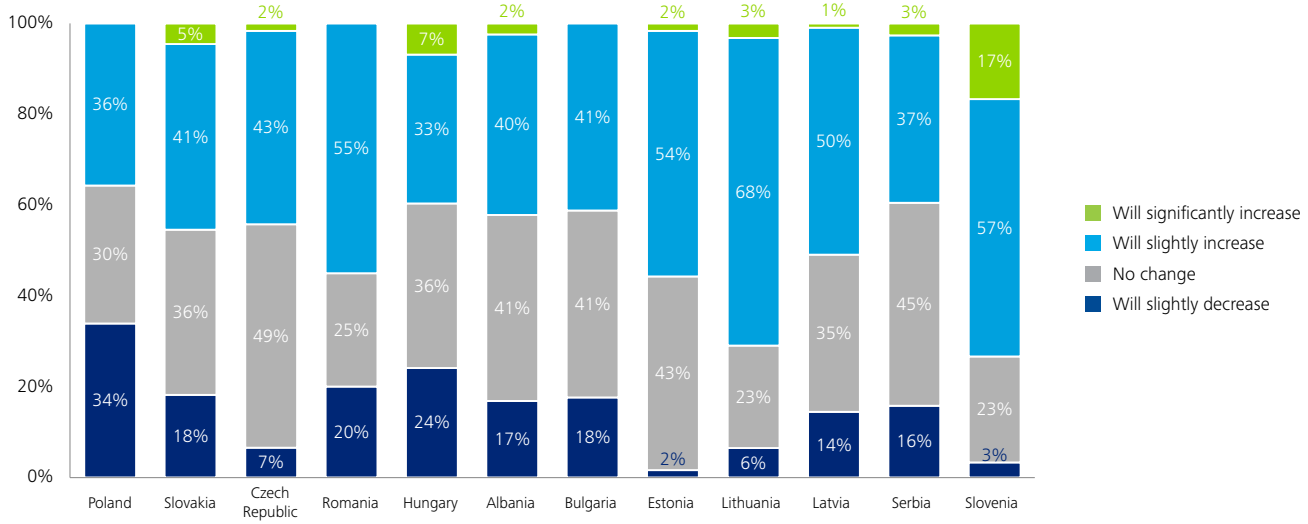


**Chart 23. Financing costs in Central Europe**

Forecast of changes in financing costs within 12 months







## Is Poland leading growth in the M&A market?

Polish CFOs expect the highest growth in the M&A market of all the countries participating in the survey. Almost 60% of them believe that the Polish mergers and acquisitions market will grow, although it should be noted that there is also a decrease in the percentage of CEOs who see opportunities for a significant increase in this area.

Such responses are consistent with an increased appetite for risk; however, they slightly contradict the very low priority accorded to investments. This is probably the result of differing perceptions of the definition of 'investment' and 'M&A'. Investments mean organic growth, which requires capital expenditure; it may be depreciated/amortised, and it can lead to increased employment. M&A is recognised as the acquisition of a complete enterprise (inorganic growth).

**Chart 24. Change in M&A level in Poland**

What changes do CFOs expect in the level of mergers and acquisitions?

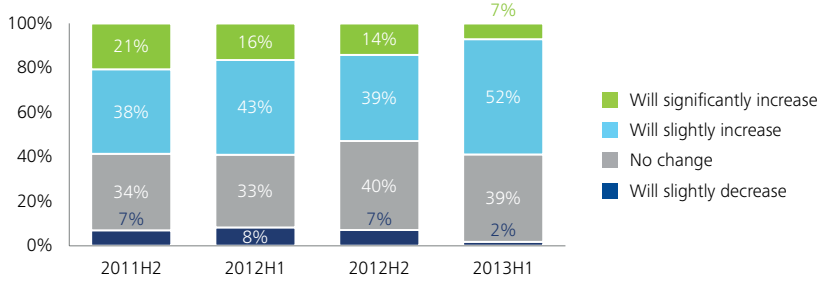
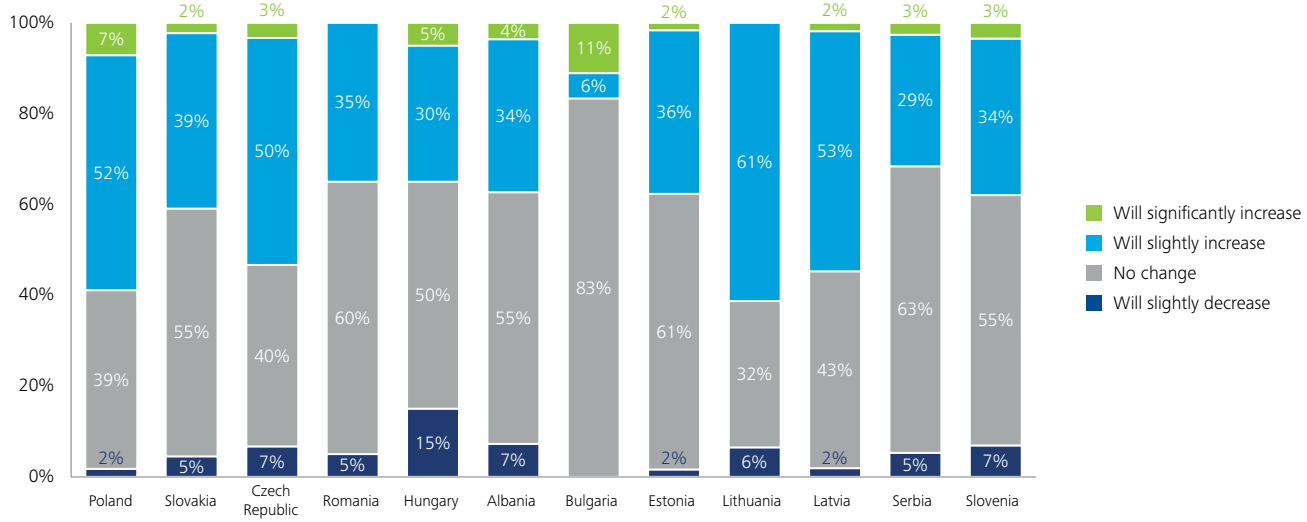



**Chart 25. Change in M&A level in Central Europe**

What changes do CFOs expect at the level of mergers and acquisitions?



# Obstacles facing business

**Comprehensive VAT procedures are the main barrier for business**

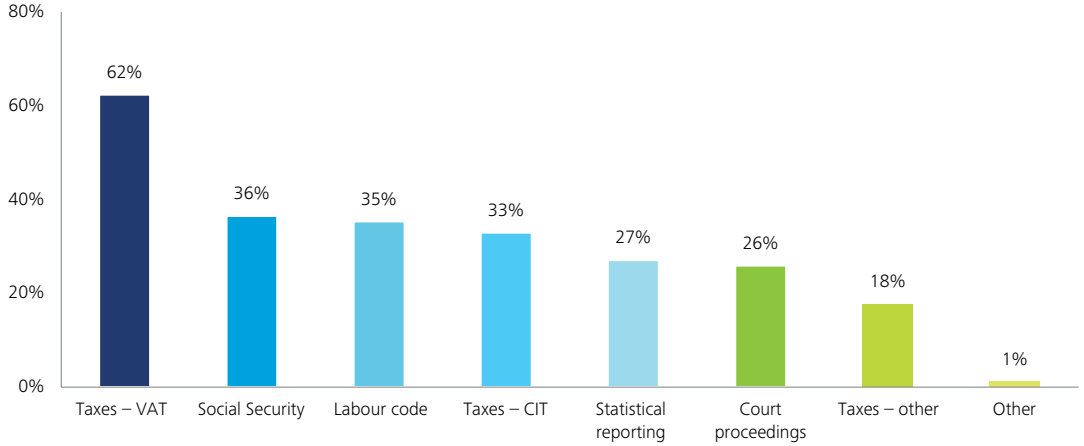
Taxes, especially VAT, are invariably the most significant problems that CFOs face. As many as 62% identify this area as the main barrier where simplification would contribute most to improving business management.

The second most significant obstacle is an area of employment law – social security and the labour code. In this period of economic uncertainty, when employment flexibility may be crucial for business survival, such aspects appear to gain additional significance.

It is also worth emphasising that, compared to the previous edition when as many as 48% of CFOs highlighted court procedures as a crucial obstacle, this percentage has decreased to 26%. This may mean that the most significant period in the liquidity crisis experienced by many survey participants has already been passed.

**Chart 26. Barriers for business**

What areas do CFOs believe to be the most important obstacles to running a business?



# Demand increases for competent financial employees

The percentage of CFOs who expect difficulties in finding good employees increased from 24% to 31%. This fact is curious in the face of increasing unemployment. Such problems appear to occur at the lower, middle and more senior parts of the hierarchy – that is, among those who already have some experience (not graduates or very senior managers). In a difficult labour market, employees themselves are probably not interested in changing jobs, leading to problems in finding attractive candidates.

The most significant problems in finding talent are in the area of controlling and financial IT systems.

**Chart 28. Labor market**

At what levels do difficulties in finding employees occur?

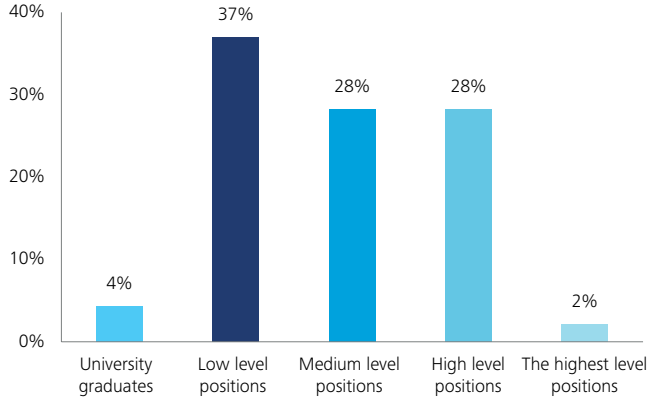



**Chart 27. Availability of employees**

Do CFOs expect difficulties in finding employees?

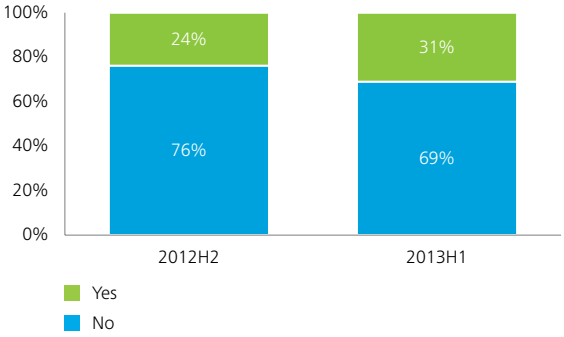
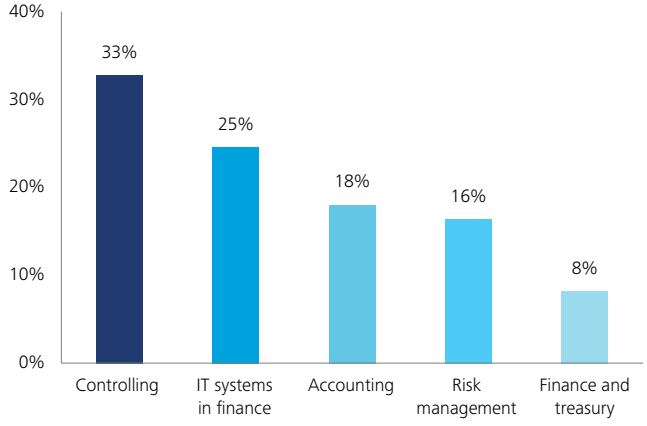



**Chart 29. Labour market**

In what areas do most difficulties in finding employees occur?



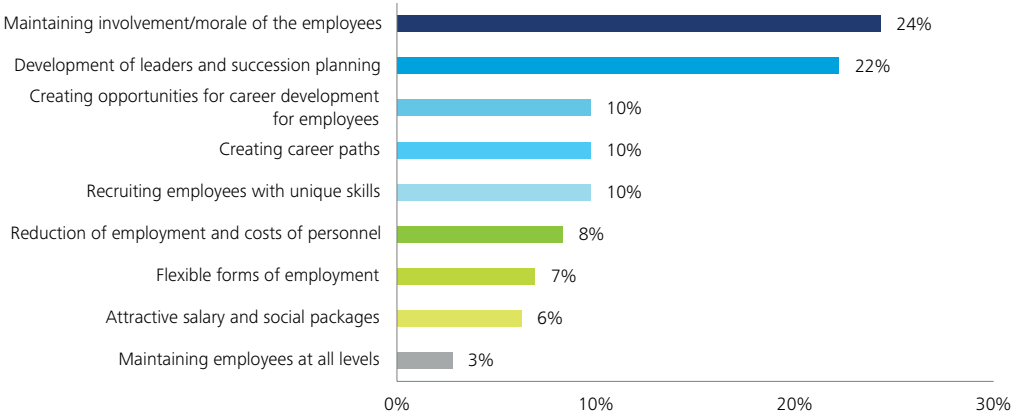
## Managing the most talented employees in finance – the challenges

In the area of talent management, the most significant challenge for CFOs is maintaining employee morale and involvement. This is especially difficult under current market conditions, when company results are not always good enough to prevent a sense of failure among employees. This can in turn lead to the threat of layoffs, which in addition negatively influences the mood of employees. However, an analysis of CFO responses shows that reducing headcount is quite far down the list of priorities. Concerns regarding job losses should therefore not be so important.

The second crucial challenge is the development of the best employees, ensuring continuity of employment and succession planning among management. The next involves providing development opportunities for all employees. The significant discrepancy in the percentage of respondents selecting these two challenges demonstrates that although ensuring general development is important, acquiring and developing true leaders is both much more important and more difficult.

**Chart 30. Talent management**

What are the most significant challenges in talent management?



# Looking into the future

### Long-term perspectives are still the best in Central Europe

There is a significant noticeable improvement in the long-term financial forecasts of CFOs in Poland. 73% (compared to just 48% in the previous survey) expect to increase their ability to service debt within three years. Moreover, practically nobody expects their own situation to worsen.

This result means that Polish CFOs still lead the way among the countries participating in the survey in terms of optimism for the next three years.

**Chart 31. Ability to service debt in Poland**

Evaluation of three-year perspective of the ability to service debt in Poland

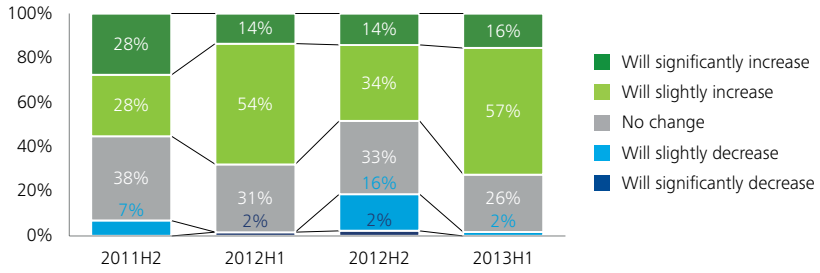
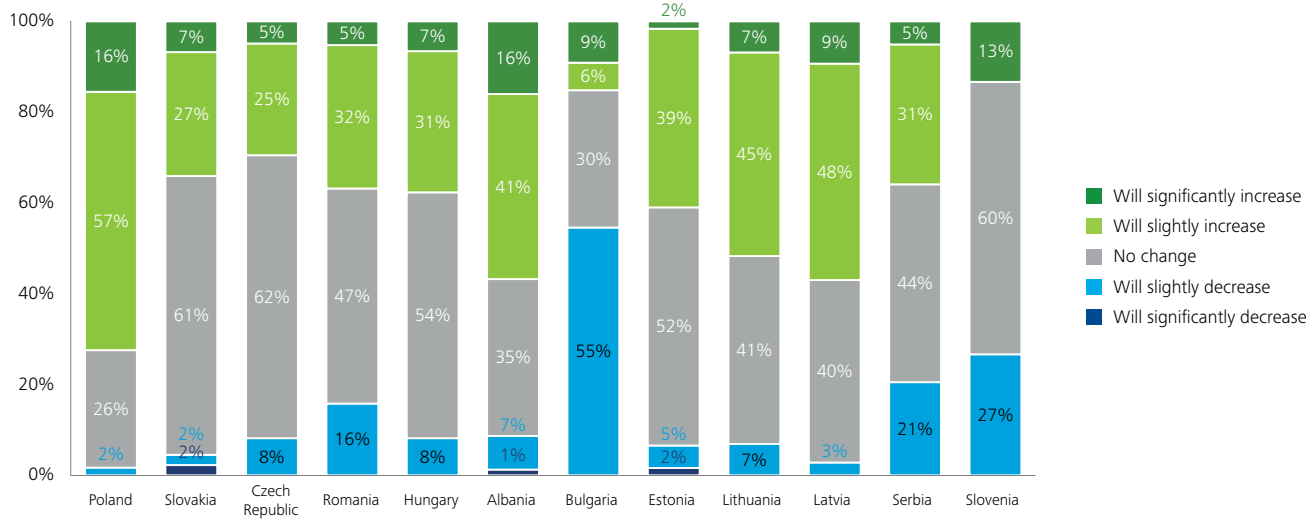



**Chart 32. Ability to service debt in Central Europe**

Evaluation of three-year perspective of the ability to service debt in CE



# Central European comparative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# The outlook for Central Europe

The global business and economic outlook is strained and under pressure. We probably have several more years of sub-par growth ahead of us. In the short term the second half of 2013 could be better than the first half but sustainable, solid growth is unlikely to return until at least 2017. Companies and CFOs need to manage their own expectations and those of their customers.

The final quarter of 2012 was extremely difficult for the global economy and for the CE region, with nearly all markets reporting significant slowdowns, but Poland and Ukraine in particular. The first quarter of 2013 has been mixed at best.

Given the business cake is not growing much globally, western companies are doing two things:

1. Moving to emerging, faster-growth markets; and
2. Engaging in best practice wherever they can. Unfortunately the CE region is performing more weakly than most other 'non-developed' markets. Core CE grew by only 0.6% last year, and we estimate that GDP growth this year will be a mere 0.8% thanks to a slower Polish outlook: for comparison, Asia Pacific will grow by 4.8% this year and Latin America by 3.4%.

Table 1: Growth trends in Central Europe

| | GDP 2013 (%) | When does GDP return to 3% | Long-term growth trend to 2023 (%) |
|---|---|---|---|
| Bulgaria | 1.3 | 2016 | 3.4 |
| Baltic States | 3.2 | now | 3.6 |
| Croatia | -0.4 | not before 2023 | 2.6 |
| Czech Republic | -0.1 | not before 2023 | 2.5 |
| Hungary | -0.1 | 2017 | 2.8 |
| Poland | 1.4 | 2015 | 3.4 |
| Serbia | 1.4 | 2018 | 2.8 |
| Slovakia | 1 | 2015 | 3.6 |
| Slovenia | -1.2 | not before 2023 | 2.4 |
| Romania | 1.3 | 2015 | 3.6 |
| Albania | 2.2 | 2014 | 3.9 |

Central Europe is next to the crumbling eurozone, and CE exports are heavily dependent on that market. The eurozone declined by -0.4% last year and this year a best case is zero growth; another mild recession of -0.5% is more likely, however. The eurozone has gone from critical illness phase to chronic debility, although crises like Cyprus intermittently raise the level to one of intensive care.

In terms of the best-performing business sectors in the CE region, these can be categorised as:

1. Pharmaceuticals and medical equipment
2. Luxury products
3. IT products and services (although these have tumbled badly in the last 15 months)
4. Retail
5. Food & beverages
6. General consumer products and FMCG
7. Beer industry (as a sub-sector)
8. B2B (engineering, manufacturing, equipment, chemicals)

**Five major factors** are holding back the global economic recovery including that of the CE region.

1. Banks are not functioning properly and not lending enough to the corporate sector and end-consumers. This is a global feature; new bank loans in the USA are a bare 2-3% of the total, but in the UK they are negative and in the eurozone close to flat while loans to SMEs are -4%. Across much of core CE region new loans are only rising by 1-2 %, while in Hungary, for example, they are down by -10% to 20%. Western investor banks are downsizing their assets in the CE region to protect their home balance sheets. Banks are also tending not to finance local CE firms, and this is making sales difficult for western and local supplier companies into the B2B sector.

2. The austerity programmes that many CE governments are currently engaged in are not balanced with any growth element, and some might argue that this is exacerbating an already weak outlook in markets such as the Czech Republic, Bulgaria and Romania. Poland is something of an exception; following an initial commitment to austerity measures in early 2012, the government has changed direction and is now working with the National Bank to support the country's crumbling GDP growth. While this might enable Poland to write out its 'mini-crisis', falling sales mean that many companies are already suffering.

3. Consumers are neither happy globally nor in the CE region: they are worried about elevated levels of unemployment, ranging from 5-8% in Romania and the Czech Republic to 14-17% in Slovakia and Poland. Indirect taxes are rising, social benefits are being cut and pensions are losing their value – so it is unsurprising that consumers fear for their future and are alienated by rampant public corruption.

*Consumer confidence indicators in selected markets in 2013 (where zero = contentment)*

| | |
|---|---|
| China | +12 (happiest people in the world) |
| Sweden | +11 |
| Germany | -5 |
| Eurozone | -23 |
| Spain | -32 |
| Greece | -72 (unhappiest people in the world) |
| Bulgaria | -42 |
| Czech Rep. | -20 |
| Hungary | -36 |
| Poland | -30 |
| Slovakia | -29 |

*Source: DT Global Business Consulting*

Household spending in most core CE markets is currently close to zero and has been strained for several years: in Hungary, household spending has been flat or negative for close to seven years, and markets such as the Czech Republic are currently reporting retail sales have fallen by 5% in the last year.

4. Companies are not spending; eurozone companies are sitting on 1.5 trillion euros because they are not confident enough to invest, to spend or to hire workers. This trend is also visible right across the CE region. If governments engage in austerity and consumers are not spending, then the future is highly uncertain. This means that companies too are not confident enough to invest and we see this in the survey results below. Uncertainty and lack of confidence are damaging company financing and the outlook of CFOs.

5. Finally, global and regional export trade slumped last year. This trend applies to ALL CE markets, but Romania is a particularly powerful example where exports have slumped brutally in recent years:

This is a significant downward slide, but it is one that reflects global/European trends. We do except a mild export recovery this year to +2.0%, but even this presumes that there is a steady recovery in the euro-zone driven by Germany; this is not guaranteed. As in other markets, industry and investment struggle when exports fall, another source of pain for the B2B sector.

Table 2: Exports (% change annually)

| Country | 2010 | 2011 | 2012 |
|---|---|---|---|
| Romania | 15% | 10% | -4.0% |
| Hungary | 12% | 6.5% | 2% |
| Poland | 15% | 7.5% | 0.5% |
| Czech Republic | 12% | 4% | 5% |
| Slovakia | 16% | 13% | 9% |

The dependency on exports has also warped the structure of some economies, of which Slovakia is a very good case study. Here, strong export growth spurred industrial output to feed external demand that provided the confidence needed for investment (but even this export growth started to slow in 2011/2012).

**Table 3: Slovakia GDP growth and by sector, 2010-12**

| | 2010 | 2011 | 2012 |
|---|---|---|---|
| GDP | 4.4 | 3.2 | 2.0 |
| Industrial output | 18.9 | 7.1 | 10.1 |
| Fixed investment | 6.5 | 14.2 | -3.7 |
| Exports | 16.5 | 12.7 | 8.6 |
| Household spending | -0.9 | -0.5 | -0.6 |

It is clear from the table above that Slovak consumers were left out of the Slovak growth story. This was because wages were not rising, companies were squeezing productivity out of the existing workforce and unemployment was elevated at 12-17%, so undermining any consumer confidence and spending.

The bad news for the Slovak economy is that exports are set to slow further in 2013 to 4%.

Overall the business outlook will remain challenging until 2016-17, given that the eurozone will be weak for at least as long.

But in terms of business the CE region does have some pluses as well as minuses:

- Brand penetration is weak, and western investors have room to expand strongly
- Companies can look to expand sales in rural areas outside the capital cities
- There are opportunities for affordable innovation of products and services in the region
- EU funding does and will provide a buttress to growth and infrastructure spending
- While south-east Europe is particularly weak, closer ties with an eventually recovering EU and improved trade links by 2015-16 will act as some support.

**The region remains attractive for out-sourcing as western firms look for service centres which are physically close to their European bases. The quality of human resources in the region is good to very good.**

# Comparative section

This section of the report compares the expectations of CFOs from the 13 Central European countries that participated in the survey (Albania & Kosovo, Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Serbia, Slovakia and Slovenia). It is based on answers of 668 CFOs from a broad range of industries.

**How CFOs are rising to the challenge**

CE businesses are operating in difficult times, so it is unsurprising that a lack of confidence permeates the responses of participating CFOs from most of the markets across the region. There are exceptions, of course – to the north of the region, the mini-boom in the Baltic states is supporting more positive attitudes to risk and expectations for the future that are above average across many metrics.

But the recent rapid slowdown of the Polish economy and continuing negative pressures in the Czech Republic are nonetheless causing uncertainty for finance professionals across the region as its two largest economies falter in the face of continued pressures among the key trading partners of Western Europe.

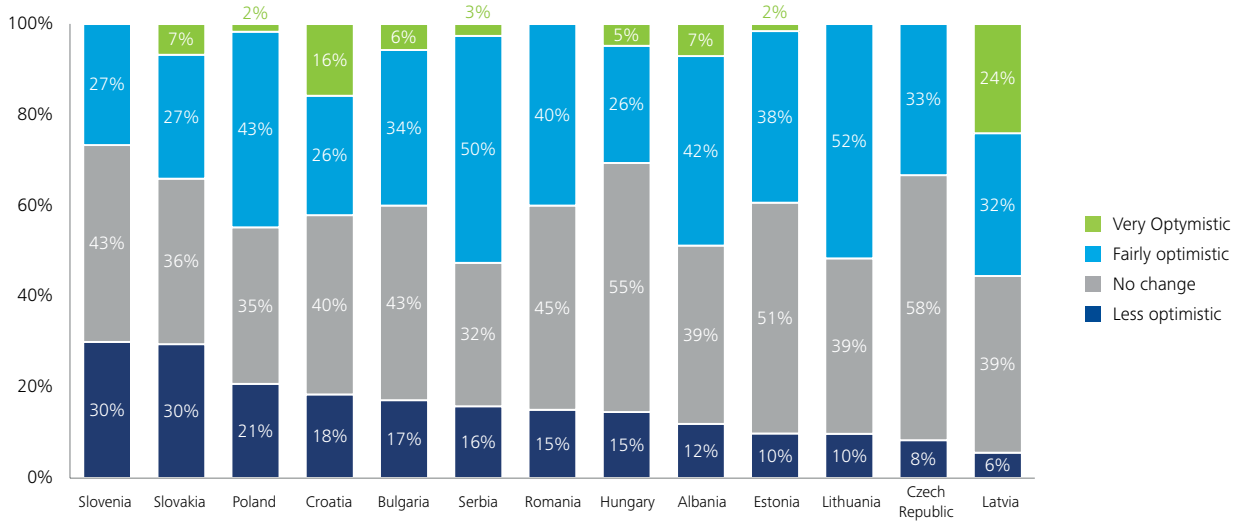
Further south, CFOs in the troubled market of Slovenia can see little prospect of improvement as the country's woes continue. Those in Hungary have only, meanwhile, raised their expectations for a less uncertain economic future because of the exceptional depths they had already plummeted.

But right across the region, embracing Bulgaria and Romania, Slovakia and Albania, Serbia and Croatia, CFOs continue to rise to the ever-evolving challenges whose roots can still be traced to the global financial crisis of 2008 and 2009. While there appears to be an emerging consensus that recovery will be well on track for most by 2017, this still represents close to a 'lost decade' for today's generation of senior financial managers. So their determination to lead their companies through such turbulent times remains impressive and inspirational.

## Optimism in short supply

Quite understandably, few companies are 'very optimistic' as there are no grounds for excessive confidence. The large number of companies who expect little change in main markets such as the Czech Republic, Hungary, Romania and Slovakia is understandable as several drivers here are static. Some 43% of Polish companies are fairly optimistic about their home market compared with six months ago. The moderate/good opinion of the Baltic markets is also understandable as these markets undergo a mini-boom as they recover from deep lows. Serbian CFOs share upbeat opinions, but again a very recent softening in this market could raise doubts.

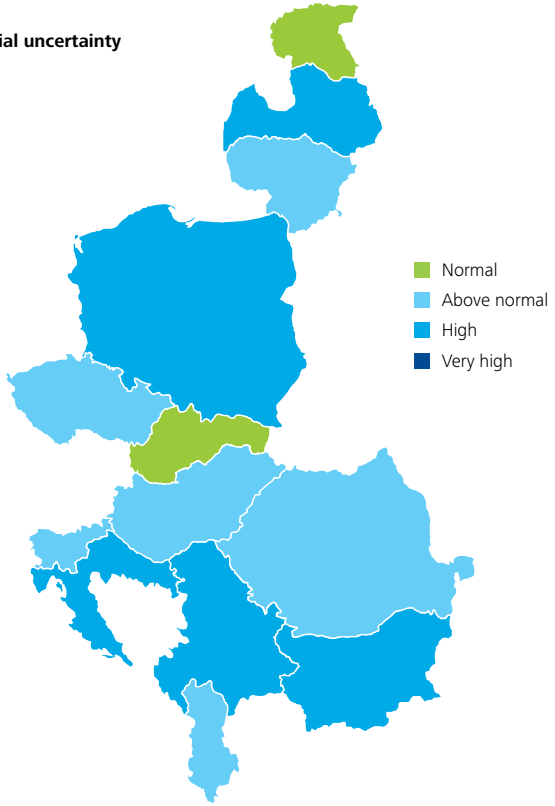
**Chart 33: Financial prospects for companies**



## Living in uncertain times

The great majority of companies express elevated levels of uncertainty, which are particularly high in Slovenia. Hungary is only less uncertain because companies have already lowered their expectations. While Croatia is feeling high levels of uncertainty as the market deteriorates, Slovakia is rightly judged as a more stable market than its neighbours. The Czech Republic has changed from a stable, even traditionally well-performing market to a much weaker one with downside risks; respondent opinions reflect this.

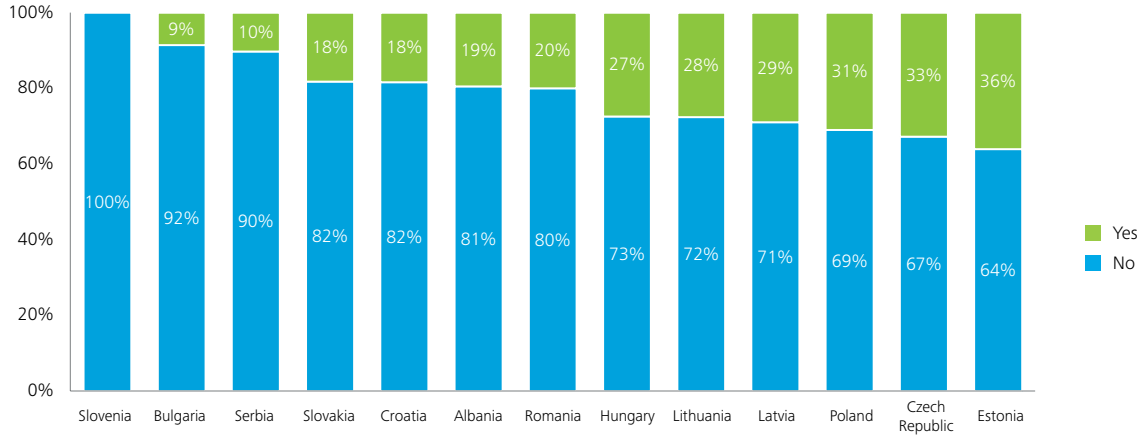
**Map 1: General level of external financial uncertainty**



## Risk-aversion rules

Right across the region, the response is perfectly clear: companies and CFOs want to avoid risk on the balance sheet. The relatively high number of Czech CFOs who feel differently may reflect the view that while the market is currently weak, now is the time for risk in the expectation of returning stability in the medium and longer terms – and the same arguments apply to Poland.

**Chart 34: CFOs' view if now is a good time to be taking greater risk onto companies' balance sheets**




## Business focus for the year ahead

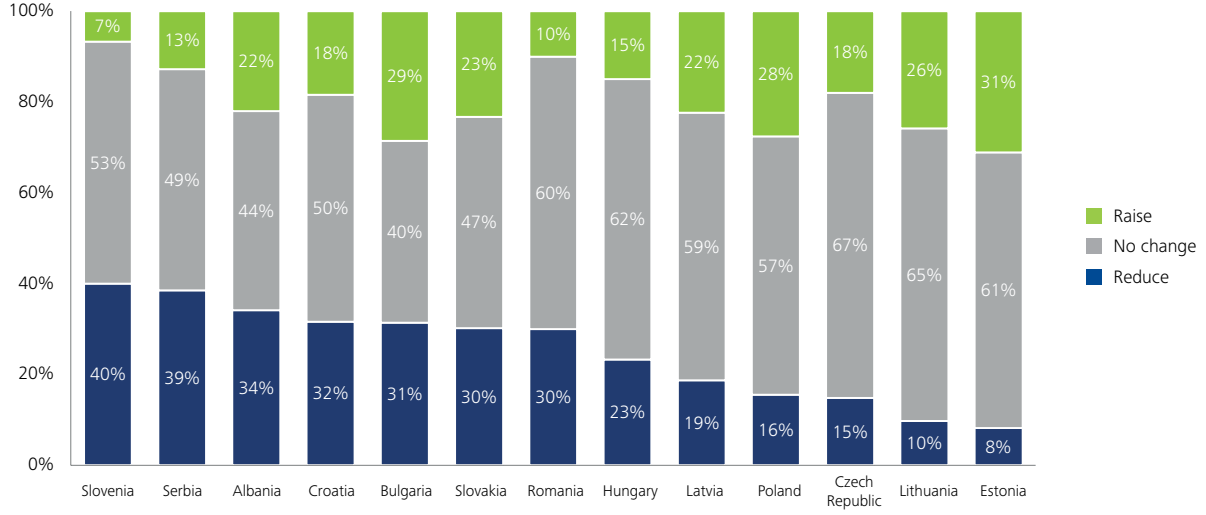
When searching for revenue growth, most CFOs across Central Europe's markets mix their priorities between domestic growth and expansion in foreign markets, which may include other core CE markets and those such as Russia and Turkey. CFOs outside Poland may be looking to the Polish market for future growth, but this remains tight and competitive.

Reducing fixed and indirect costs is important to most CFOs in the core CE markets; an exception is Poland. However, cost reduction is increasing even here. Again, the Baltic states are more focused on growth at the moment than cost cutting. Improving liquidity remains moderately important or more across nearly all CE markets.

## Gearing up for no change?

Most CFOs remain cautious on the subject of gearing, with large majorities in most markets anticipating no change. Poland and the Baltics emerge as markets where gearing may be raised, while around 40% of CFOs in Slovenia and Serbia are planning to reduce their gearing.

**Chart 35: CFOs' aim for the level of gearing over the next 12 months**

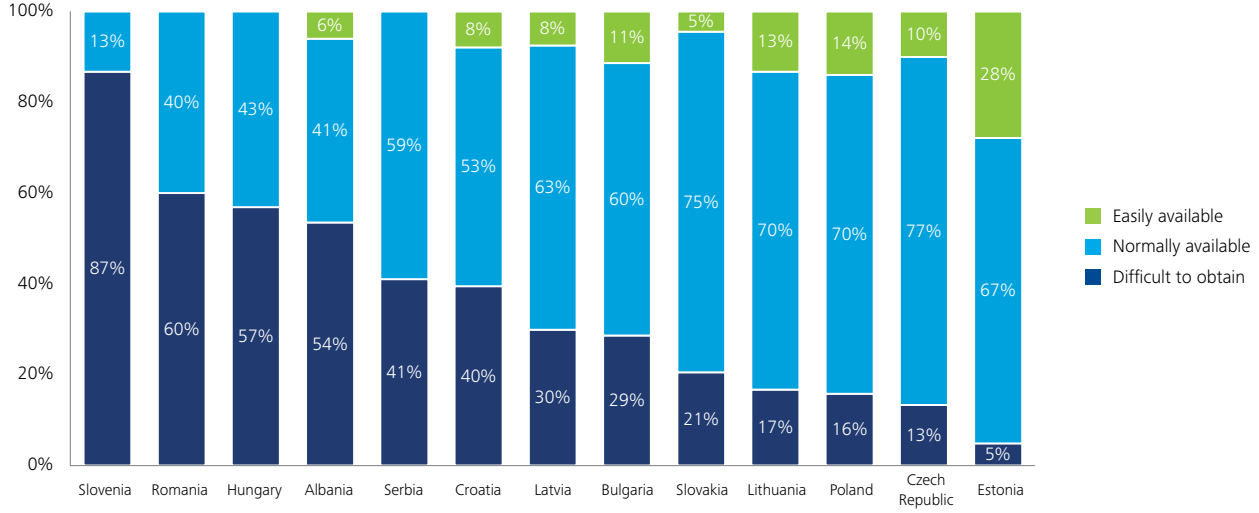


## A mixed credit picture

It is a pleasant surprise that so many CFOs rate new credit as 'normally available' given the low amounts of new credit released in most core CE markets. Some of this response may be due to companies not wanting to borrow, but feeling that funds are 'on the table' if required.

That said, in Hungary, Romania and Albania more than half CFOs state that new credit is hard to find, which echoes common complaints in these markets. The worst situation seems to be in Slovenia, where almost 90% of CFOs claim that credit is difficult to obtain.

**Chart 36: Overall availability of new credit for companies nowadays**

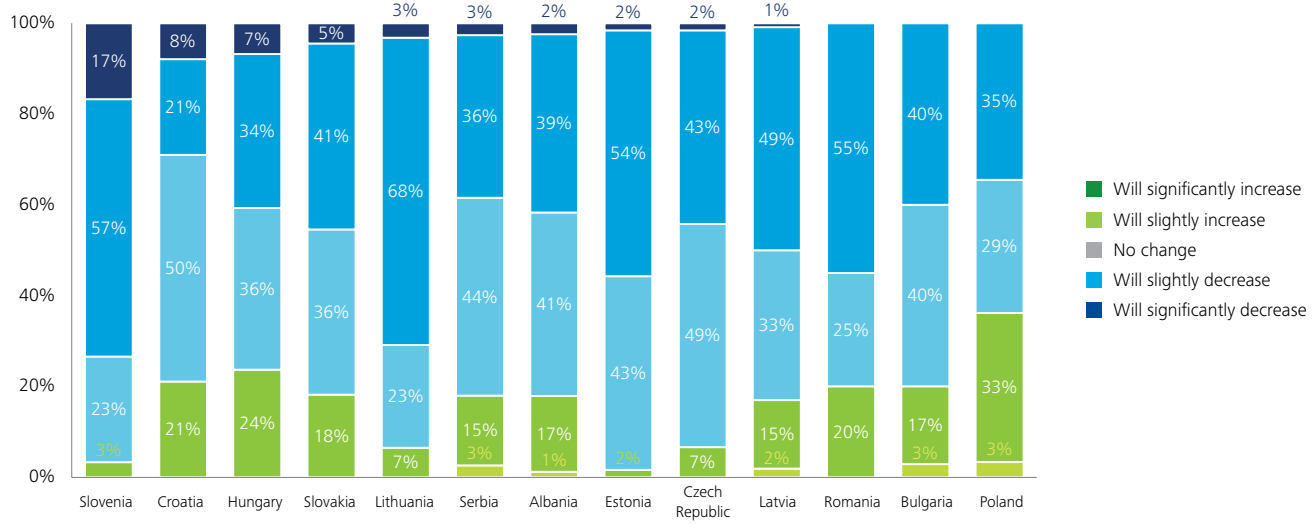


## Recovery will drive up finance costs

Broadly, CFOs feel that the costs of finance are set to rise. Interest rates are low or very low in most markets; rates will start to rise, possibly slowly, whenever the economic cycle picks up, and this is reflected in most responses.

One exception is Poland where the National Bank is embarking on a cycle of interest rate cuts in response to the country's sharp economic slowdown.

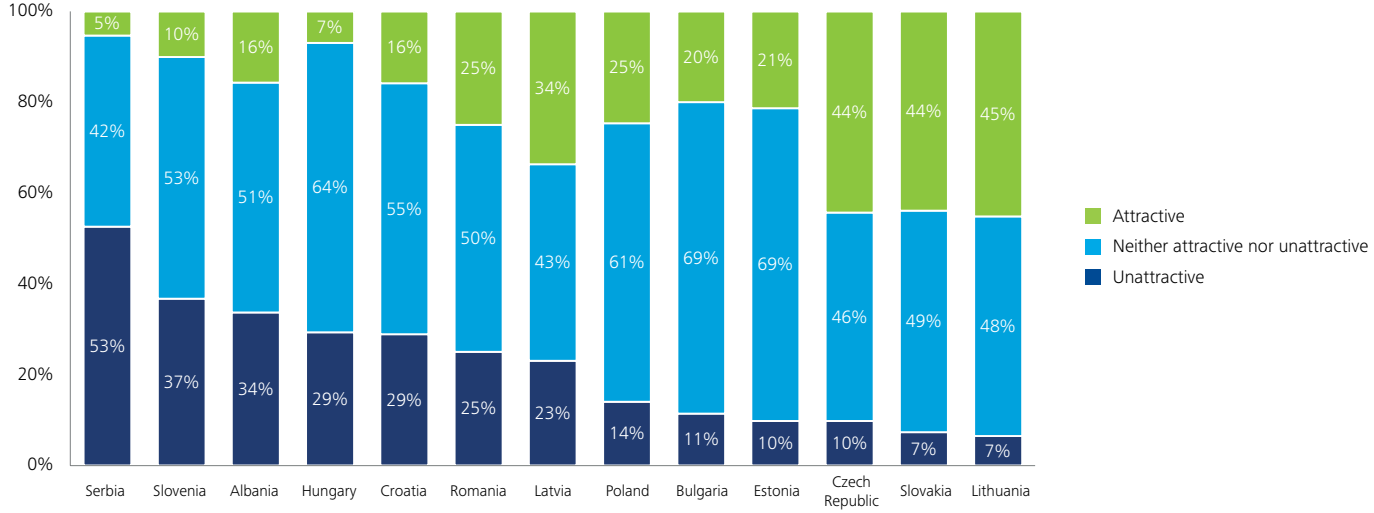
**Chart 37: Expected change in financing costs for companies over the next 12 months**



## Most CFOs are banking neutral

Most CFOs are neutral about the attractiveness of bank borrowing. This fits in with the financing and growth picture across the region, with its combination of banks not lending and some companies not wanting or needing to borrow. Several markets across the region, such as the Czech Republic, Slovakia and Lithuania regard it as more attractive than others, but there is no discernible logical pattern and variations are probably driven by specific corporate needs in those markets.

**Chart 38: Attractiveness of equity raising as a source of funding**

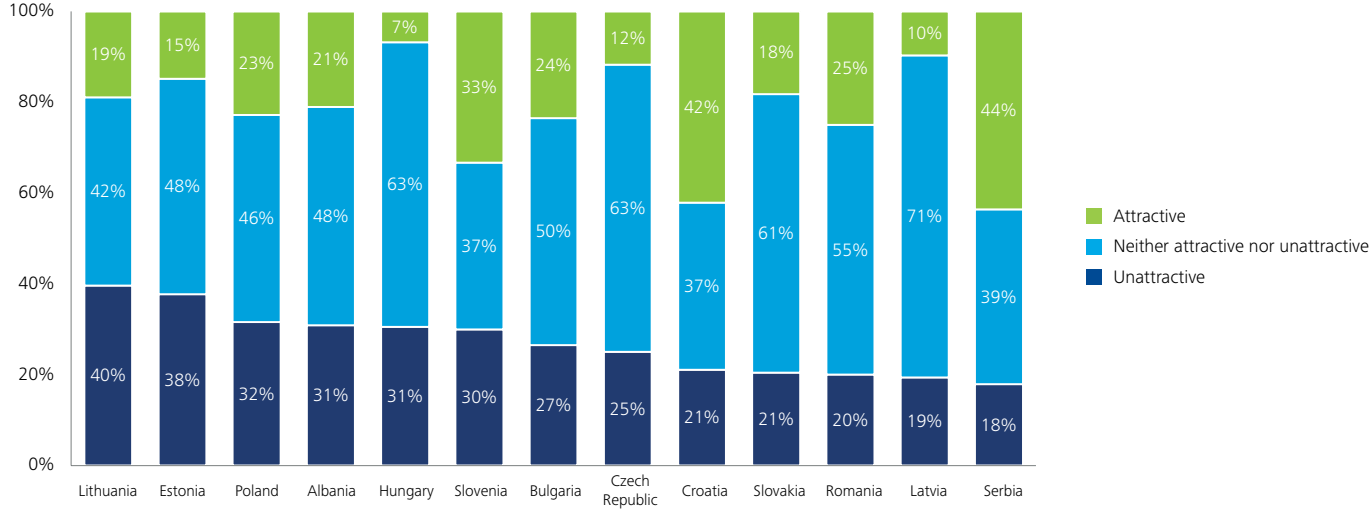


## Opinions split on equity funding

Most CFOs currently find raising equity as neither an attractive nor an unattractive source of funding, but those in Croatia, Serbia and Slovenia stand out as mild exceptions and those in Latvia find it less appealing.

Responses from Poland are quite mixed, which reflects the country's shifting economic direction and increasing uncertainty.

**Chart 39: Attractiveness of equity raising as a source of funding**

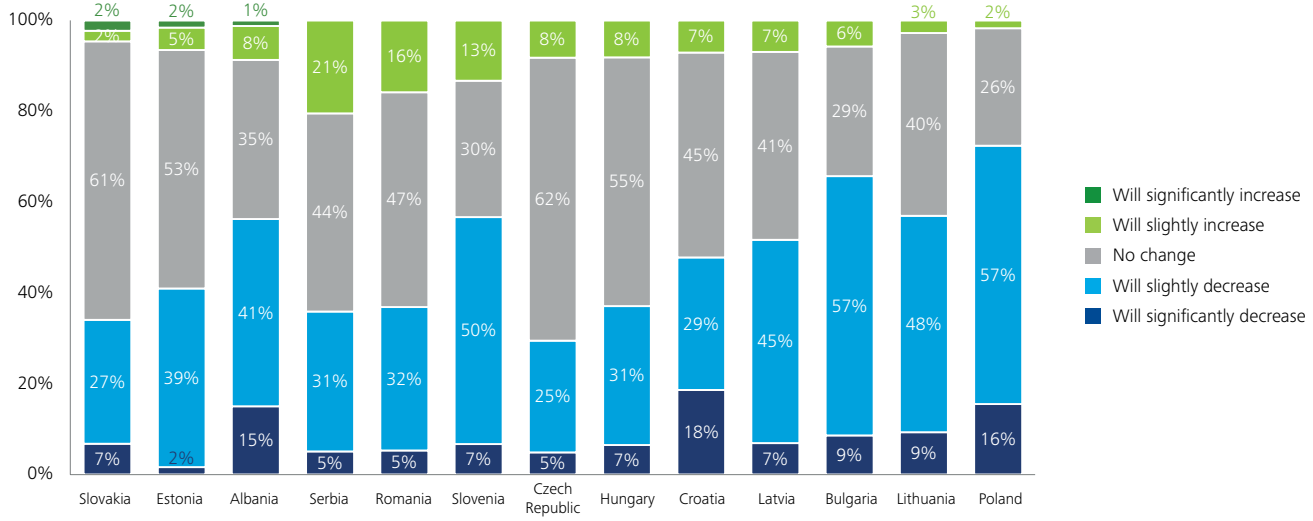


## Servicing debt

Regarding companies' ability to service their debt, responses are much as expected: most CFOs predict an unchanged environment while almost the same proportion expects an improvement.

This is based on the view that markets will improve moderately over the next three years. Rising interest rates may prove a hindrance here, but it appears unlikely that rates will rise fast enough to be a problem in this period.

**Chart 40: Expected change in companies' ability to service their debt over the next 3 years**

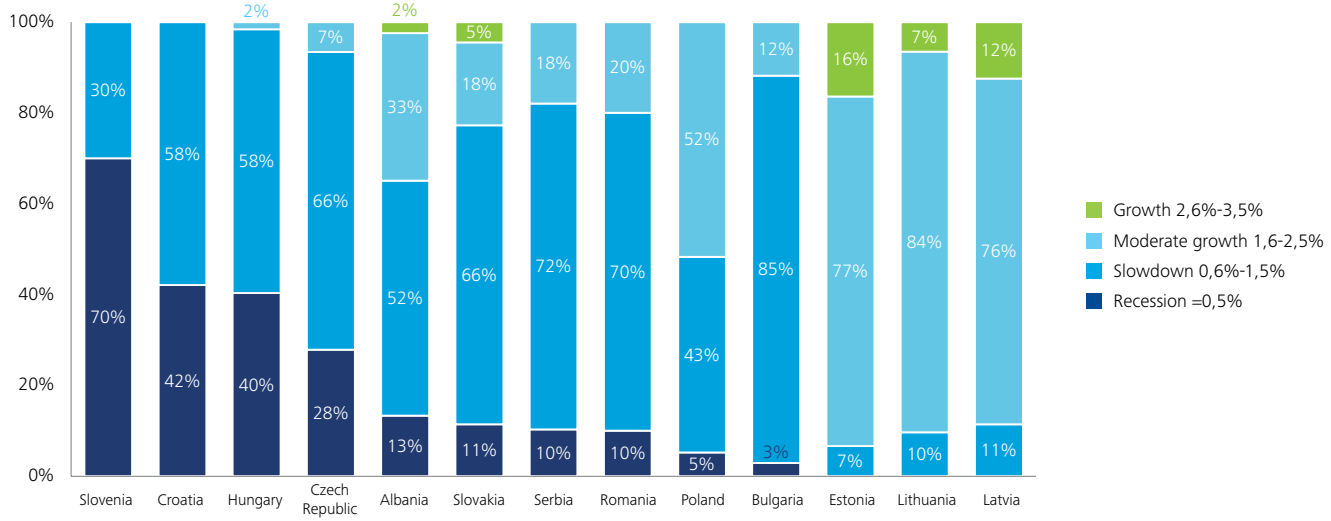


## Expectations for growth

CFOs expect low single-digit GDP growth across the region, with a weaker performance expected in the Czech Republic, Croatia and Hungary and a somewhat stronger than average return from the small Baltic markets.

As last year, Slovenia is once again the most pessimistic country in the sample, with 70% of CFOs expecting recession.

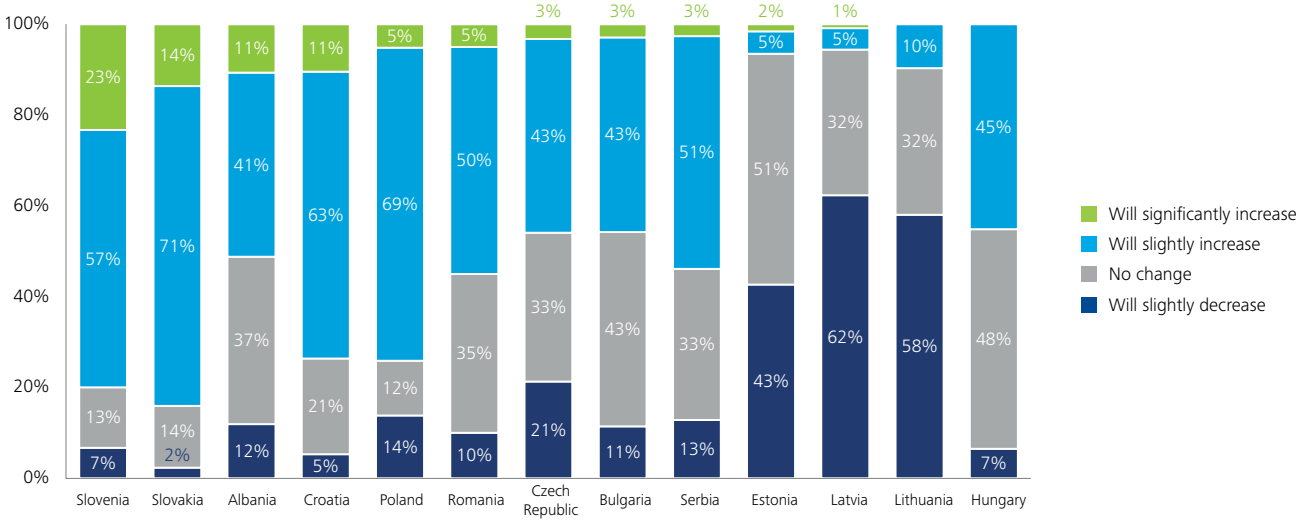
**Chart 41: CFOs' expectations for the country GDP growth in 2013**



## Expectations for unemployment

Most CFOs expect unemployment to increase somewhat or at best remain neutral in most markets; the exception is the again Baltic states, where a majority of CFOs forecasts that unemployment will fall.

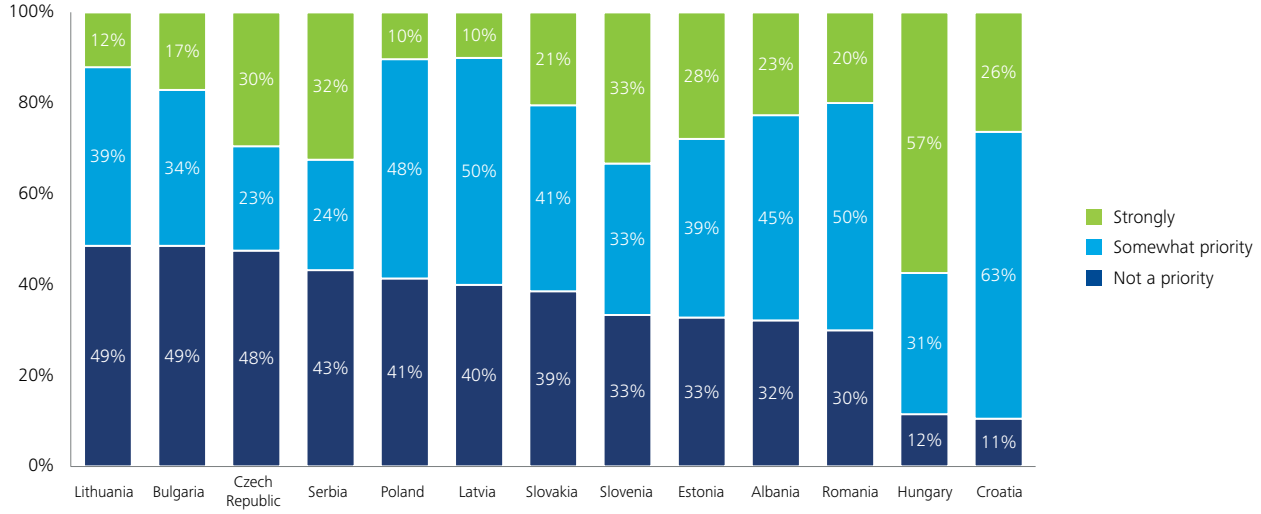
**Chart 42: Expected change in unemployment level over the next 12 months**



## A question of remodelling

CFOs are split as to whether remodelling or restructuring will be a priority for their business in the near future. This partially reflects a desire to remain stable as they wait and see how things develop; it is also partly because much has already been done in most markets. Hungary and Slovenia stand out as two markets where one third to more than half of executives expect to remodel; in Slovenia, this relates to the possible need for a bail-out and even a longer-term recession, while in Hungary the ongoing slump and government regulations also encourage further right-sizing. CFOs will also monitor developments in the Czech Republic and Croatia to see whether they need to downsize or, in Croatia's case, adapt to the EU.

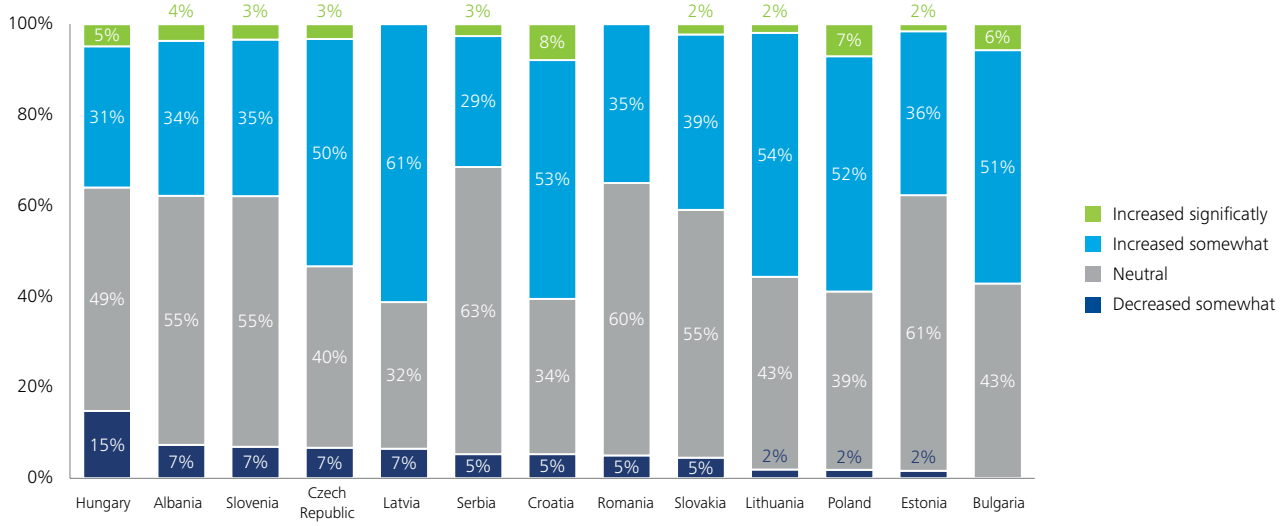
**Chart 43: Expectations to what extent is business remodelling or restructuring likely to be a priority for your business over the next 12 months**



## A marginal increase in M&A?

Regarding M&A, the respondents' outlook fits with their responses to other questions. In fact, with almost half of executives replying that they will see some slight increase in M&A this year, there is a marginally optimistic view. Some of this anticipated M&A activity will be due to sales of distressed assets, Western investors divesting and private equity playing a larger role. Again, however, almost half the CFOs from across the region expect the flat trend to continue. Moderately increased activity in Poland could be due to executives responding to the current slowdown by planning to buy and sell.

**Chart 44: Expected change in M&A levels over the next 12 months**

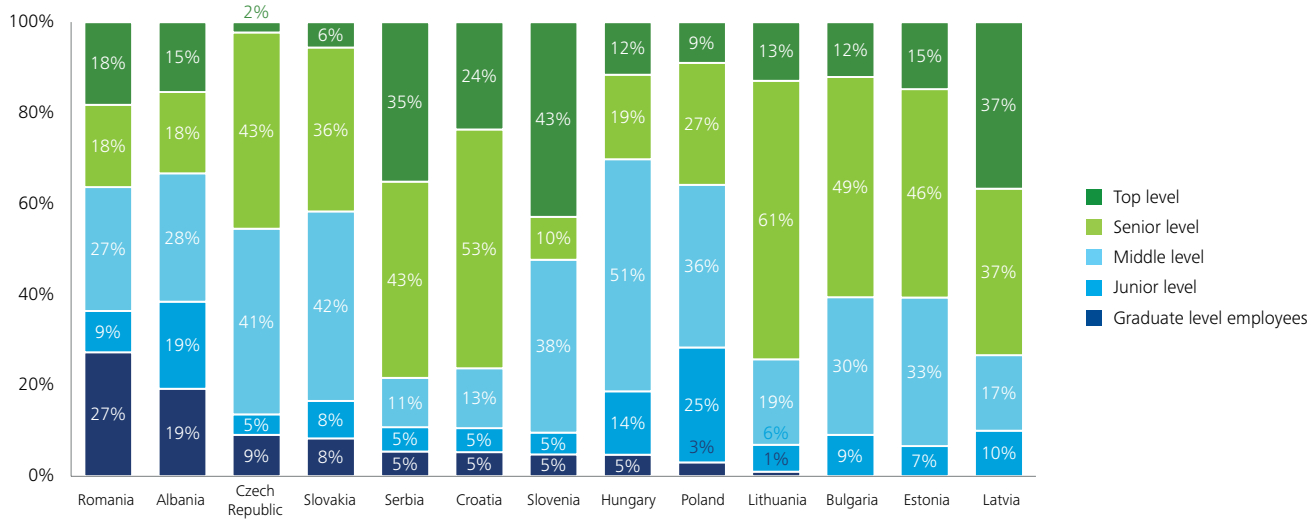


## Talent in finance

Around two thirds of all respondents do not expect any talent shortages in financial roles across the region. This makes sense; there is not much of a talent shortage at the moment, and a fragile business outlook puts most power in the hands of the employers. (For comparison, this is not the case in Russia where talent shortages exist across the board and salaries remain elevated.)

That said, almost one third of CFOs do feel that there will be shortages, and this possibly includes top-quality people in key roles. This conclusion is reflected in the final question of the survey, where CFOs indicate that shortages will apply to the more senior levels. However, Romania and Albania stand out with 28% and 19% of CFOs respectively predicting quite significant talent shortages at the graduate level, which contrasts with the other countries.

**Chart 45: Expected talent shortages in finance over the next year**



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## Methodology

The 4th CFO Survey took place between the 18th of February and the 1st of April. A total of 668 CFOs across 13 countries completed our survey. The survey is divided into two parts, first - local analysis based on responses from Poland and the second part is based on all the responses across the region. Not all survey questions are reported in each bi-annual survey.
If you were interested to see the full range of questions, please contact ifiserova@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.