CFO Insights | Japan
2018 Q2

Contents

Japan Economic Outlook:
Economy shows signs of rebound

Growth trends: Economy recovers on the back of strong consumer spending

The Japanese economy appears to be rebounding after a decline in real gross domestic product (GDP) in the first quarter of 2018. Real (inflation-adjusted) GDP increased at an annualized rate of 1.9 percent from the first to the second quarter.[1] This follows a contraction of 0.9 percent in the first quarter. Second-quarter growth was the fastest since the third quarter of 2017.

Real consumer spending grew at an annual rate of 2.8 percent, while investment in housing fell at an annual rate of 10.3 percent. In- vestment by business was up at a very strong rate of 5.2 percent. Exports were up at a modest rate of 0.8 percent, while imports grew at a strong rate of 3.9 percent. Thus, it appears that, at least for the second quarter, growth in Japan was likely more a function of domestic demand than of exports, a shift that the government was hoping to see. Moreover, this is welcome because there is considerable risk to the global trading system, given the burgeoning trade war

1 Cabinet Office, Government of Japan, Quarterly estimates of GDP for April–June 2018, August 10, 2018.

between the United States and China, both important trading partners for Japan. The revival of consumer spending is likely due to the tightness of the labor market and the positive impact of this on household income. The rise in labor costs has likely compelled businesses to invest in "labor-saving" technology, thus boosting capital spending.

Retail sales were up 1.8 percent in June versus a year earlier, the fastest rate of increase since December 2017.[2] Sales rose strongly at department stores, and moderately at general merchandise and food stores; they fell at apparel stores and automotive dealerships. Nonetheless, sales were up very strongly at petrol stations, reflecting the sharp increase in energy prices from a year ago. Whether retail sales growth will be sustained in the months ahead will depend in part on how the economy responds to very low unemployment. Currently, at 2.2 percent, unemployment is at a 25-year low.

Policy: Central bank assures "continuous powerful monetary easing"

Many investors were concerned about the potential impact of the policy meeting of the Bank of Japan (BOJ) in late July. They anticipated a significant shift in monetary policy that could lead to much higher bond yields and a stronger yen. Indeed, concerns were such that yields rose enough for the BOJ to intervene in the market on three occasions to prevent the 10-year yield from rising above 0.1 percent.

Nonetheless, investor concerns eased after the BOJ indicated that nothing much had changed. Rather, the BOJ statement mentioned that the bank will pursue continuous powerful monetary easing[3] and that it will keep interest rates historically low. Moreover, the BOJ intends to maintain low interest rates "for an extended period of time." This kind of forward guidance, common for some central banks, is new for the BOJ. The central bank's governor, Haruhiko Kuroda, said that its statements "will fully counter speculation among some market participants that the bank is heading [toward] an early exit or an increase in rates." In response to the news, Japanese bond yields fell as the value of the yen fell as well.

The BOJ has maintained an unusually aggressive monetary policy for several years, which involved negative interest rates and massive asset purchases—so much so that the BOJ's balance sheet is now 98 percent of the GDP compared to the US Federal Reserve's 20 percent. Yet despite this aggressive posture, inflation remains historically low in Japan. The BOJ remains confident that inflation will eventually rise to the bank's target. It stated that "the momentum

2 Trading Economics, "Japan retail sales 1971–2018," accessed August 20, 2018.

3 Leo Lewis, Kana Inagaki, and Emma Dunkley, "BoJ defies global move to roll back crisis-era stimulus," Financial Times, July 31, 2018.

toward achieving the price stability target of 2.0 percent is maintained but is not yet sufficiently firm." Japan is characterized by deflationary psychology and a declining population, both of which likely contribute to very low inflation.

Trade: Government takes steps to mitigate possible risks from the US–China trade dispute

One of the biggest risks to the Japanese economy stems from the US–China trade dispute. Japan's manufacturing and technology sectors could be hurt if the dispute were to cause a significant disruption to Asian supply chains. As such, it is not surprising that Prime Minister Shinzo Abe has stated that Japan intends to boost its economic relations with China.[4] This is seen as a possible response to US protectionism. Japan stands to be hurt by US tariffs on Chinese goods, many of which include Japanese components. Thus, from Japan's perspective, it makes sense to find ways to reduce its exposure to the United States. Japan clearly wants to boost exports to China, while China would likely want to see more Japanese investment in China. The latter would be helpful in improving the technical capabilities of the Chinese industry.

Meanwhile, although Japan wants to boost its economic relations with China, it is wont to see China dominate trading relations in the region. As such, Japan has played a key role in reviving the dormant Trans-Pacific Partnership (TPP), which was sidelined after the United States withdrew from it in January 2017. Japan, Australia, Canada, and the other original signatories to the TPP have agreed to pursue free trade, in part as a way to offset the efforts of China to organize trade in the region.

Author information: Ira Kalish is a specialist in global economic issues based in Los Angeles, California.

4 Peter Landers, "Strange bedfellows: Trump trade fight brings Japan and China together," Wall Street Journal, June 18, 2018.

Accounting News

IFRSs

Revised Conceptual Framework

In March 2018, the IASB published its revised Conceptual Framework for Financial Reporting. Included are revised definitions of an asset and a liability as well as new guidance on measurement and derecognition, presentation and disclosure.

Together with the revised Conceptual Framework, the IASB has also issued Amendments to References to the Conceptual Framework in IFRS Standards. The document contains amendments to IFRS 2 Share-based payments, IFRS 3 Business Combinations, IFRS 6 Exploration for and Evaluation of Mineral Resources, IFRS 14 Regulatory Deferral Accounts, IAS 1 Presentation of Financial Statements, IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, IAS 34 Interim Financial Reporting, IAS 37 Provisions, Contingent Liabilities and Contingent Assets, IAS 38 Intangible Assets, IFRIC 12 Service Concessions Agreement, IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments, IFRIC 20 Stripping costs in the Production Phase of a Surface Mine, IFRIC 22 Foreign Currency Transactions and Advance Consideration, and SIC-32 Intangible Assets-Web Site Costs. Not all amendments, however update those pronouncements with regard to references to and quotes from the framework so that they refer to the revised Conceptual Framework. Some pronouncements are only updated to indicate which version of the framework they are referencing to, or to indicate that definitions in the standard have not been updated with the new definitions developed in the revised Conceptual Framework.

The amendments, where they actually are updates, are effective for annual periods beginning on or after 1 January 2020.

For additional information, see our related IFRS in Focus newsletter as well as the IASB press release and our IAS Plus project page on the IASB's conceptual framework project on the amendments.

No other new standards, amendments or interpretations were issued by the IASB during this Quarter.

U.S. GAAP

The FASB has issued several Accounting Standards Updates, including:

Accounting Standards Update No. ("ASU") 2018-04 — Investments – Debt Securities (Topic 320) and Regulated Operations (Topic 980): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 117 and SEC Release No. 33-9273 (SEC Update)

This ASU incorporates amendments made to SEC guidance that is included within the accounting standards codification. For more information, see this ASU as included on the FASB's website.

ASU 2018-05 — Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118 (SEC Update)

This ASU incorporates amendments made to SEC guidance that is included within the accounting standards codification. For more information, see this ASU as included on the FASB's website.

ASU 2018-06 — Codification Improvements to Topic 942, Financial Services – Depository and Lending

This ASU supersedes obsolete guidance in Topic 942 that is related to the Office of the Comptroller of the Currency's Banking Circular 202, "Accounting for Net Deferred Tax Charges," because that guidance has been rescinded by the Office of the Comptroller of the Currency and is no longer relevant. For more information, see this ASU as included on the FASB's website.

Japanese GAAP and other local developments

The ASBJ issues the Exposure Drafts of Proposed Amendments to Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries, etc. for Consolidated Financial Statements and related Practical Solution

In May 2018, the ASBJ issued for public comment the following two Exposure Drafts:

- Proposed Amendments to PITF No.18 Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries, etc. for Consolidated Financial Statements (Exposure Draft of PITF No.55)

- Proposed Amendments to PITF No.24 Practical Solution on Unification of Accounting Policies Applied to Associates Accounted for Using the Equity Method (Exposure Draft of PITF No. 56)

The ASBJ proposed to amend the accounting treatment for 1) gain or loss on sale of equity instruments, which are held by foreign subsidiaries, etc. and designated as FVTOCI and 2) impairment loss of those equity instruments, in preparing the consolidated financial statements of the parent company.

The comment are due on 30 July 2018.

The ASBJ issues amendments to 'Japan's Modified International Standards (JMIS): Accounting Standards Comprising IFRSs and the ASBJ Modifications'

In April 2018, the ASBJ issued amendments to JMIS in order to mainly reflect the endorsement process on IFRS9 (2014).

JMIS are standards and interpretations issued by the IASB with certain "deletions or modifications" where considered necessary by the ASBJ. The ASBJ issued JMIS in June 2015 and has examined the accounting standards issued by the IASB since then. To date, JMIS has been issued as a result of the endorsement process covering IFRS15 as well as the Standards issued by the IASB as at 31 December 2016 which became effective by 31 December 2017.

For this round, the ASBJ undertook the endorsement process on the amendments made by IFRS9 (2014) and the Standards issued by the IASB as at 30 June 2017 which become effective on or after 1 January 2018, except for IFRS16 *Leases* and IFRS17 *Insurance Contracts*.

For more information, see the press release and related documents on the ASBJ website.

The ASBJ issues a new revenue standard, which is largely based on IFRS15 'Revenue from Contracts with Customers'.

In March 2018, the ASBJ issued Standard No.29 *Accounting Standard for Revenue Recognition*, which builds on the core principle of IFRS15 and the main model to apply the principle (the five step model).

Although the new revenue standard is not identical with IFRS15, the standard development by the ASBJ did not result in significant impairment of international comparability. Still, there are several departures in the areas including contract cost accounting, multiple alternative treatments applicable only under the Japanese revenue standard, disclosure provisions, etc. Until the standard has been applied by companies and the degree to which they will use the alternative treatments is known, it is not clear what the departures will sum up to in the end.

The new standard and its related implementation guidance in Japanese are available on the ASBJ's website.

The Financial Service Agency (FSA) of Japan announces that additional

designated IFRSs for use by companies voluntarily applying IFRSs in Japan.

In March 2018, the FSA announced the update to the list of "designated" IFRSs that are issued by the IASB by 31 December 2017. The "designated" IFRSs are for use by companies that voluntarily apply IFRSs in Japan. **Prepayment Features with Negative Compensation (Amendments to IFRS9), Long-term Interests in Associates and Joint Ventures (Amendments to IAS28) and Annual Improvements to IFRS Standards （2015-2017 Cycle）** were proposed to be newly reflected on the list.

The ASBJ issues Tentative Practical Solution on Accounting for Virtual Currencies under the Payment Service Act.

In March 2018, the ASBJ issued the PITF No. 38 *Tentative Practical Solution on the Accounting for Virtual Currencies under the Payment Service Act* in response to the Japanese Payments Services Act amended in 2016 as well as increasing recognition of virtual currencies as a means of payment.

The PITF No.38 addresses the accounting for virtual currencies as defined in the Payment Services Act and builds on two decisions on 1) whether virtual currencies are assets or not and 2) what type of assets virtual currencies are.

For more information, see the short summary of the practical solution on the ASBJ website.

The ASBJ issues Tentative Practical Solution Regarding the Effective Periods of PITF No.34.

In March 2018, the ASBJ issued the PITF No.37 to extend the effective period of PITF No.34, which permits an accounting policy choice regarding the discount rate to be used in accounting for the post-retirement benefits under the current market, where negative interest rates can be observed. As a result of this tentative practical solution, PITF No.34 can be applied for the time being unless the ASBJ identifies necessity to reconsider the effective period.

The ASBJ meets the Italian standard-setter in their 2nd Biannual Meeting.

In April 2018, the ASBJ and the Italian standard-setter Organismo Italiano di Contabilità (OIC) held a joint meeting in Rome. The meeting was the second bilateral meeting between the two standard-setters. For more information about the meeting, see the press release on the ASBJ website.

The ASBJ meets the Australian Accounting Standards Board (AASB).

In March 2018, the ASBJ and AASB held a meeting in Melbourne and updated each other on their respective financial reporting frameworks and activities. For more information about the meeting, see the press release on the ASBJ website.

The ASBJ meets the Hong Kong Institute of Certified Public Accountants (HKICPA) in Hong Kong to

discuss higher quality accounting standards by collaboration.

In March 2018, the ASBJ and the HKICA held the first bilateral meeting to discuss various type of issues, including their projects on developing the accounting for group reorganisation (or intra-group mergers and acquisitions) and the accounting for virtual currencies. For more information about the meeting, see the press release on the ASBJ website.

For more information, please visit: IASPlus.com (IFRS) or USGAAPPlus.com (U.S. GAAP) or speak to our Deloitte experts Takafumi OSEKO, Partner (takafumi.oseko@tohmatsu.co.jp) or ALEJANDRO Saenz, Senior Manager (alejandro.saenzmartinezgeijo@tohmatsu.co.jp).

Tax News

Recent reforms impacting deductions of foreign stock compensation granted to directors

Overview

"Compensation paid to a director is, in principle, not deductible for Japanese corporate tax purposes. However, there are exceptions for the following:

Fixed Compensation – compensation paid in equal instalments at least monthly;

Pre-Notified Compensation – compensation for which the company notifies the tax authority in advance regarding the compensation to be paid to a director; or

Performance-Linked Compensation – compensation based on performance provided certain conditions are met. Generally, only publicly traded Japanese companies are eligible under this category."

Also, regardless of whether or not the compensation paid to a director falls under one of the above exceptions, if such compensation is considered as excessive, the excessive portion will be disallowed as a deduction.

Further, parent company stock compensation (e.g. stock options, restricted stock, etc.) granted to directors of a subsidiary was generally not eligible to qualify for one of the above exceptions. However, since the 2016 and 2017 tax reforms entered into effect, certain parent company stock compensation issued to directors of a Japanese subsidiary became eligible for deduction provided it can fall into one of the above mentioned exceptions.

Please note that the rules regarding the deductibility of stock compensation under Japanese corporate tax law discussed in this newsletter relate to stock compensation granted by a Japanese company. There are no specific tax laws addressing stock compensation granted by a foreign parent company.

However, while there is some uncertainty, in practice and under the right circumstances, the rules for Japanese stock compensation may be applied to foreign stock compensation.

1. Tax reforms

(1) Qualifying restricted stock eligible for Pre-Notified Compensation under 2016 tax reform

Under the 2016 tax reform, restricted stock compensation granted by a parent company to a director of a 100% owned Japanese subsidiary qualified as Pre-Notified Compensation provided certain conditions (including that the compensation be for future services to be rendered by the director, restrictions are imposed on the transfer of such stock for a certain period, and certain disclosures are made on the subsidiaries corporate tax return) are satisfied. In addition, an advance notification would need to be timely filed, but such notification may be exempted under certain situations.

(2) Expanded scope of Pre-Notified Compensation under 2017 tax reform

Under the 2017 tax reform, parent stock compensation treated as Pre-Notified Compensation was expanded to include stock options with a fixed number of shares to be issued at a pre-determined time provided such options had a market price.

Further, the ownership threshold of the parent company granting the stock compensation dropped such that parent stock compensation granted to a director of a more than 50% owned Japanese subsidiary became eligible for treatment as Pre-Notified Compensation. An example of stock compensation that may be classified as Pre-Notified Compensation is stock options that require a director to continue to be a director for a specified number of years before such options vest with the director and can be exercised. In addition, an advance notification would need to be timely filed, but such notification may be exempted under certain situations.

However, any stock compensation that that is granted based on the director's performance should not be classified as Pre-Notified Compensation (even if other conditions are satisfied), but instead, as Performance-

Linked Compensation and eligible for a deduction only if the conditions associated with the Performance-Linked Compensation category are satisfied (i.e. submitting an annual report to the Japanese finance bureau with details of the compensation). In general, it is difficult for Japanese subsidiaries of foreign multinationals to satisfy this condition.

2. Key procedures to qualify as Pre-Notified Compensation

(1) Legal procedures

Generally, total director compensation (including stock compensation) should be approved during a shareholder's meeting of the Japanese subsidiary, however, once total compensation is approved, each individual director's compensation amount can be determined by a meeting of the directors.

Please note that any director compensation in excess of what is approved at the shareholder's meeting is generally not deductible for Japanese corporate tax purposes.

Regarding foreign parent stock compensation, a recharge agreement should be established such that the Japanese subsidiary burdens the costs of the stock compensation granted by its parent company.

(2)Advance notification

Advance notification generally must be submitted to the tax office within one month from the date of a shareholder's meeting or director's meeting that resolves the director compensation (if directors start working before that date, the working start date) or 4 months from the beginning of fiscal year, whichever is earlier.

The advanced notification requires the following information to be included:

name of directors to which stock compensation is granted,

- date of grant,
- name of issuing company,
- number of shares or stock options granted,
- fair market value of stock compensation etc.

Deloitte's View

While many types of stock compensation issued by a foreign parent company to directors of its Japanese subsidiary remain non-deductible (e.g. stock compensation based on performance), companies should not automatically assume that the stock compensation offered to their directors is non-deductible and they may want to reexamine their stock compensation program to determine whether it already meets the conditions to be treated as Pre-Notified Compensation or whether some amendments can be made to meet such conditions. For example, it is not uncommon for a foreign multinational company to have a global compensation program designed to enhance the performance of, and retain, its directors worldwide by offering stock compensation. To the extent such program focuses more on the retention of the directors (i.e. grants certain stock compensation based purely on the condition that the director remain with the company for a number of years rather than based on the performance), the stock compensation granted under such program may be deductible with advanced notification.

Given that the advanced notification creates some additional compliance and requires disclosure of information regarding directors receiving the stock compensation, some companies may be hesitant to proceed with the advance notification. However, it should be noted that much of the information requested may be required to be reported by the company anyway under a separate tax law that requires companies to report to the tax authorities all vested foreign stock compensation provided to employees and directors.

For more information, please speak to our Deloitte experts Kazumasa YUKI, Tax Partner (kazumasa.yuki@tohmatsu. co.jp), or David BICKLE, Tax Partner (david.bickle@tohmatsu. co.jp).

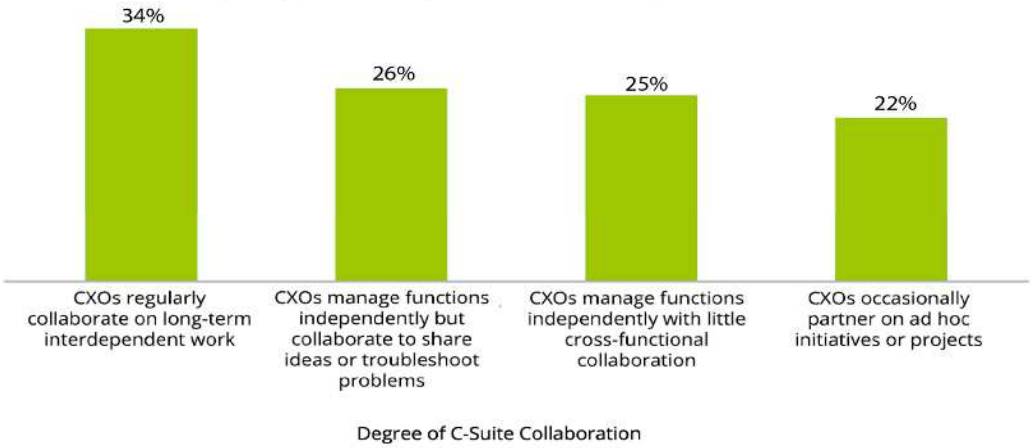
Rise of the Symphonic C-suite

As the business landscape becomes more competitive and digital disruption continues, many organizations have become more team-centric, networked, and agile. While more collaborative and flexible approaches are taking hold in sales, operations, and other functional areas, however, a big problem remains: The C-suite sometimes lags, operating as an independent collection of functional experts rather than as a coordinated team.

The issue is common enough that 51 percent of respondents to [Deloitte's 2018 Human Capital Trends] report identify C-suite collaboration as very important—making it the most critical issue in this year's survey. In addition, respondents at organizations with the highest level of CxO cross-collaboration are the most likely to anticipate growth of 10 percent or more (Figure 1). Stunningly, however, 73 percent of respondents say their C-suite leaders rarely, if ever, work together on projects or strategic initiatives.

Figure 1: Influence of C-Suite Leadership Style on Company Growth

Share of each cohort expecting growth of 10 percent or more in each year



Source: Deloitte *Global Human Capital Trends* Survey, 2018

The survey points to a significant opportunity for senior leaders to pursue a new, more collaborative, team-based model — the symphonic C-suite. Like a great symphony orchestra, a symphonic C-suite brings together multiple elements: the musical score (the strategy), the different types of instrumental musicians (the business functions), the first chairs (the functional leaders), and the conductor (the CEO). In this model, C-suite members lead their own areas of responsibility but also collaborate with other functional leaders, work on teams that affect the enterprise's strategic direction, and influence networks of teams throughout the organization. In short, the goal is a symphony of specialized experts playing in harmony.

A Turning Point

The model is a departure from the way C-suites have historically behaved. In the 1800s and early 1900s, CEOs stood alone at the top, making most of the important decisions and delegating responsibility to functional managers in the business. By the 1980s, the number of functional C-suite roles — such as CFOs, CIOs, and chief human resource officers (CHROs) — increased, with each having responsibility for his or her domain and operating under a divide and conquer model.

With this increased specialization, however, a new dynamic emerged: Individual CxOs did not, as a rule, work closely together. This made sense in a relatively static, predictable business environment, where most problems had readily identifiable root causes, were limited in scope and required deep functional expertise to solve. However, the current business landscape is a far cry from that of the 1980s. Frequent marketplace disruptions, a global economy, and the accelerating rate of technological change mean that the challenges companies face often are more complex, with multiple roots and drivers that cannot be solved effectively by one party working alone.

'The movement toward the symphonic C-suite is proving to be one of the most powerful and urgent trends for organizations worldwide.'

In such an environment, pairing cross-disciplinary collaboration and deep functional expertise makes a great deal of sense, allowing leadership teams to tackle issues that no single function can satisfactorily address. For example, today's digitally savvy, well-informed consumer demands that businesses deliver good products and a rewarding end-to-end customer experience. Rising to this challenge requires that organizations understand and fulfill customer needs at every touchpoint — which takes close partnership across functions.

The Symphonic C-suite in Action

Symphonic C-suites might configure and reconfigure themselves to address different types of challenges.

—For example:

Digital business models. The transition to digital business models is at the top of the strategic agenda for many businesses today. A high-performing digital business aims to deliver its products and services to customers as an integrated experience. To achieve this goal, the CMO and CIO can work together so that front, middle, and back-office systems converge to provide a seamless customer experience.

The future of work. Organizations have a growing opportunity to redesign work and workforces to integrate robotics and AI and to capitalize on new employment models such as gig workers and crowds. CIOs and CFOs can partner with business leaders, supply chain executives, and the CHRO to implement automation solutions and redesign work to create meaningful jobs, careers, and development opportunities.

Brand protection. In a connected and transparent world, customers and employees are inextricably linked to corporate brand. CMOs and CHROs, along with the chief risk officer, can collaborate to manage an organization's total internal and external brand.

Innovation. Chief innovation officers and chief research officers can play a critical role in driving innovation across functions and throughout the business. C-suite members can work together to ensure successful innovations are shared throughout the organization and learnings are applied to other initiatives.

Cultivating the Symphonic C-suite

The transition of C-suites to full "symphonic" mode still appears to be in its infancy. Fifty-four percent of the respondents to the 2018 Global Human Capital Trends survey say their companies are not ready, or are only somewhat ready, for the level of executive team collaboration they believe is now required.

Where can C-suites start? A first step is for the CEO to review priorities for each C-suite leader and determine how each can drive progress more broadly across the organization. Next, cross-disciplinary projects can be prioritized so that CxOs can form specific alliances and coordinate their efforts. Last, executive teams can put cross-disciplinary projects on the agenda and communicate their collaborations to the rest of the workforce as a model to follow.

As companies execute this shift, teamwork, influence, and expertise become more important. Finding leaders who create fellowship among their peers may require organizations to assess talent in new ways. Achieving C-suite collaboration also requires performance management systems and career paths that facilitate teaming and provide leaders cross-functional experience. Deloitte's survey shows that CxOs with experience in a greater number of functions prior to reaching their current level are more likely to indicate that their organization's C-suite regularly collaborates.

Organizing Around the Symphonic C-suite

The movement toward the symphonic C-suite is proving to be one of the most powerful and urgent trends for organizations worldwide. CxOs at leading companies understand that working as a team is now essential, and they are beginning to reorganize around this model. This trend is likely to accelerate as organizations begin to recognize that the symphonic C-suite is the most effective way to tackle the complex issues businesses face today.

—Produced by Erica Volini, principal, and Jeff Schwartz, principal, Deloitte Consulting LLP; and Josh Bersin, founder and principal, Bersin by Deloitte, Deloitte Consulting LLP

CXOs Optimistic, Uncertain About Industry 4.0

"Many senior business executives and government agency leaders from around the world lack confidence in their organizations' readiness to influence and harness the opportunities offered by the Fourth Industrial Revolution, or Industry 4.0 — the marriage of physical and digital technologies such as analytics, artificial intelligence, cognitive computing, and the internet of things."

A recent Deloitte Global **survey** of more than 1,600 C-level executives in 19 countries found that although executives conceptually understand the changes Industry 4.0 is expected to bring, they're less certain about how to take action to benefit from those changes.

Just 14 percent of respondents say they're highly confident their organizations are ready to fully leverage Industry 4.0 to help customers, employees, communities, and other key stakeholders.

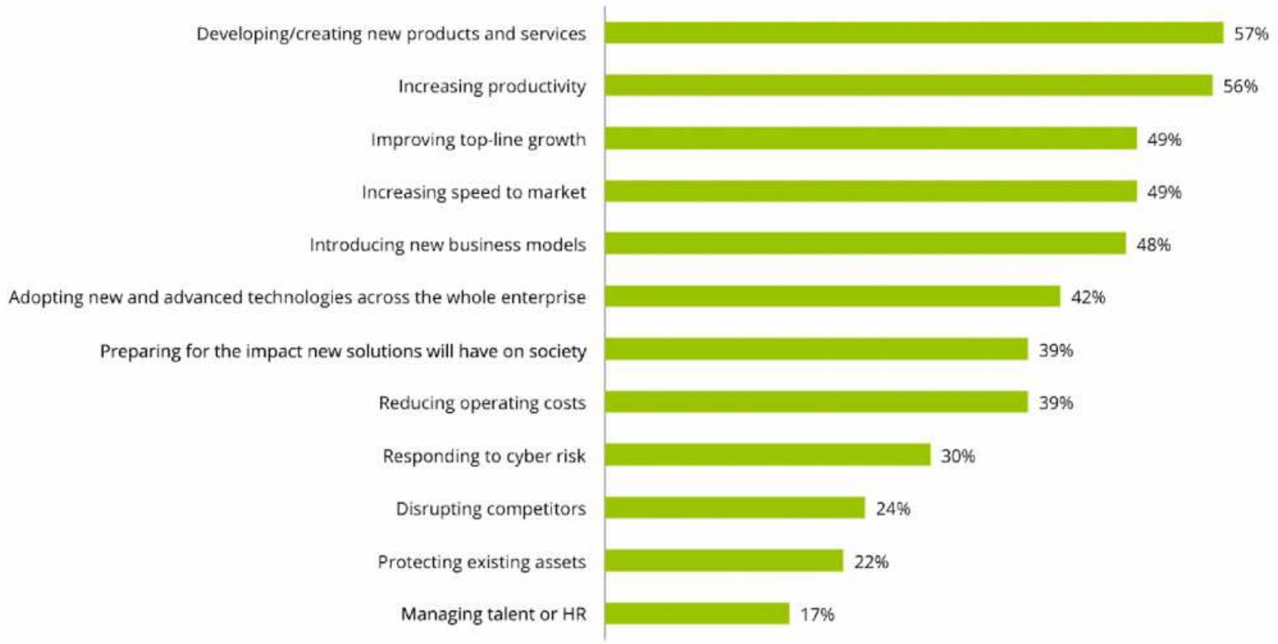
To explore Industry 4.0 readiness, the survey focused on four major areas of impact: strategy, talent and workforce, technology, and society."

—Strategy

Survey respondents' perceived lack of readiness has not compelled them to alter current business strategies. Many organizations continue to focus on traditional business operations rather than opportunities to create new value for their stakeholders. For example, developing business products and increasing productivity top the list of topics that survey participants say are discussed most frequently within their organizations (Figure 1).

Figure 1: Business Priorities Fail to Fully Address Industry 4.0

Over the course of a year, what topics do you discuss most frequently as an organization? (Select up to five)



Source: Deloitte Global / The Fourth Industrial Revolution is Here—Are You Ready?

These are important issues for Industry 4.0 — one of its hallmarks is developing innovative products and services and increasing productivity by using new technologies and data created by connected objects. However, Industry 4.0 can offer opportunities for innovation that go beyond products and services, potentially requiring new approaches to talent, cyber risk, and competitive disruption — issues that fall to the bottom of the list of priorities.

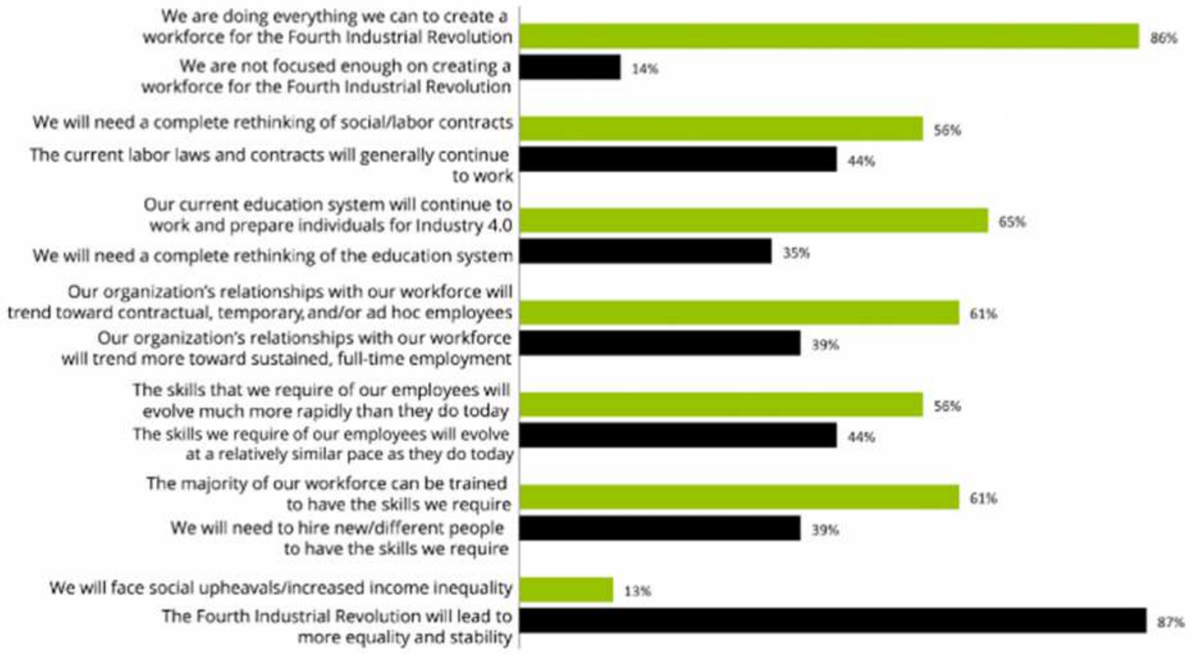
—Talent and Workforce

Survey respondents lack confidence that they have the right talent in place to be successful in Industry 4.0. Only one-quarter are highly confident they have the workforce composition and skill sets needed for the future, and just 7 percent consider their organizations highly capable of planning for and addressing the effects technology-driven changes may have on their organizational structures and employees.

Yet most executives do not express urgency when it comes to tackling the challenge of the future workforce, with only 17 percent of respondents naming talent and HR a frequently discussed topic within the organization. Most are not planning radical workforce changes to meet changing demands. A vast majority (86 percent) say they are doing everything they can to create a workforce for Industry 4.0, while 65 percent say they can rely on the current education system to properly prepare and equip workers, and 61 percent believe their existing employees can be retrained as needed (Figure 2).

Figure 2: Executives Resist Radical Workforce Development Changes

In each of the following pairs, which of the statements about the Fourth Industrial Revolution's impact on the workforce is truer?



Source: Deloitte Global / The Fourth Industrial Revolution is Here—Are You Ready?

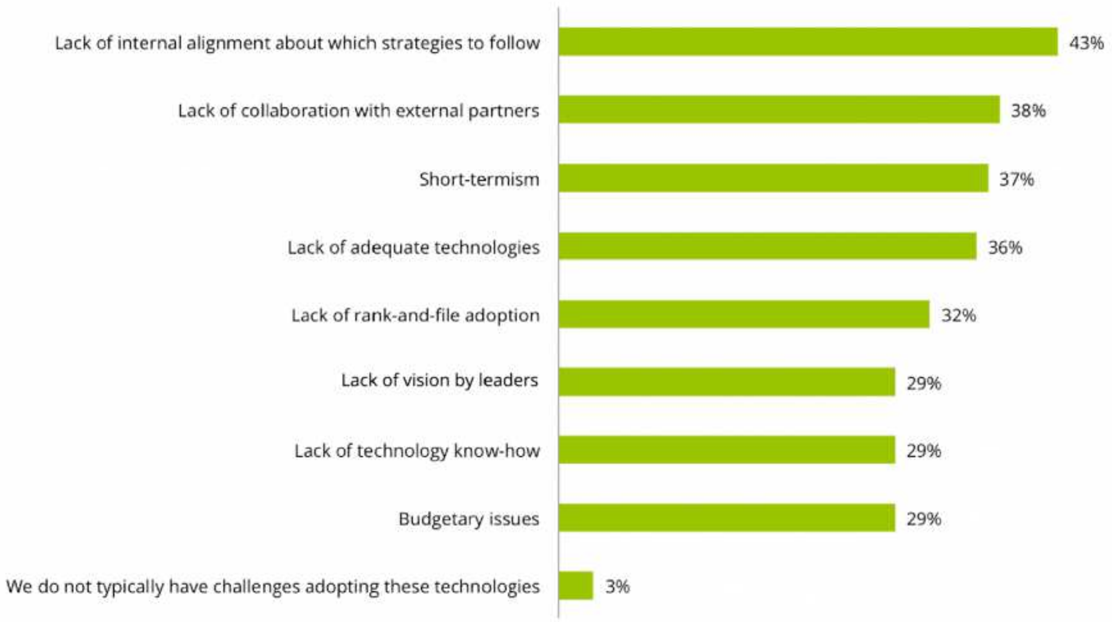
—Technology

In Industry 4.0's early stages, many organizations have become highly adept at using digital technologies to do what they have always done, only faster and better. Forty-seven percent of executives consider their organizations highly capable of using advanced technologies to help enable employees to be more efficient. However, leveraging the full transformational potential of Industry 4.0 can also require taking a broader perspective about how to use smart, connected technologies.

Only 20 percent of CXOs surveyed consider their organizations highly prepared to handle new business or delivery models, and 15 percent believe they are highly prepared for smart and autonomous technologies. Executives understand they need to invest in technology to drive new business models; however, they have a hard time making the business case for that investment. When asked what the hindrances were, 43 percent of executives point to a lack of internal alignment, while 38 percent cite a lack of collaboration with external partners, and 37 percent point to a focus on the short term (Figure 3).

Figure 3: A Challenging Business Case for Industry 4.0 Tech Investments

What are the most common challenges your organization faces as it seeks to adopt new technologies and their applications? (Select up to three)



Source: Deloitte Global / The Fourth Industrial Revolution is Here—Are You Ready?

—Social Impact

While survey respondents envision a more stable future with less inequality, they are less convinced they or their organizations will play a role in influencing society.

CXOs overwhelmingly (87 percent) believe Industry 4.0 will lead to more social and economic equality and stability, and nearly three-quarters (74 percent) say public businesses will have much more influence than governments (45 percent), nongovernmental organizations (25 percent), or other entities in shaping this future.

Yet in spite of their optimism, surveyed executives believe little is significantly within their organization's control beyond the ability to deliver the best possible products or services to customers (60 percent). Less than one in five believe their own organizations have much influence over critical factors such as social mobility (17 percent), education (12 percent), and sustainability (10 percent).

In this age of unprecedented global social and economic connectivity, the Fourth Industrial Revolution is happening quickly. Many CXOs understand it will bring dramatic changes, yet they are less certain about how to take action. If leaders choose to think more broadly and act decisively, their organizations may play a leading role in ensuring Industry 4.0 acts as a positive force.

– Produced by Punit Renjen, Deloitte Global CEO

Caesars Entertainment CFO Eric Hession, on Making a Turnaround[5]

In October 2017 Caesars Entertainment Corporation (Caesars) announced the emergence from Chapter 11 bankruptcy of one its operating subsidiaries, Caesars Entertainment Operating Company (CEOC). Buoyed by a simpler operating structure, reduced leverage, strong cash flow, and significant investment in its properties, the Las Vegas-based casino/entertainment provider announced plans to pursue a diversified growth strategy underpinned by literally a wide range of initiatives. Eric Hession was promoted to CFO of Caesars just as CEOC was entering Chapter 11 in 2015, and played a pivotal role in its emergence. He talks about the valuable

[5] —Editor's note: This article is part of an ongoing series of interviews with CEOs, CFOs, and other executives. Eric Hession's participation in this article is solely for educational purposes based on his knowledge of the subject, and the views expressed by him are solely his own. This article should not be deemed or construed to be for the purpose of soliciting business for Caesars Entertainment, nor does Deloitte advocate or endorse the services or products provided by Caesars Entertainment.

lessons learned along the way, and what's ahead for the company.

Q: Bankruptcy poses many challenges for CFOs. What were some of the things you focused most closely on?

Hession: One critical element was ensuring that our management team and operations group weren't demoralized or distracted by what we were going through. We made sure that everyone understood that the company was not going to be dissolved and shut down, that they would still be paid, and that we were continuing to invest in the business. We tried to communicate very clearly and openly that it was not an operational issue but rather a capital structure one.

I hosted conference calls with Mark Frissora, Caesars Entertainment CEO, where employees could dial in and listen to management discuss what the restructuring entailed. We explained that it was about having too much leverage, that operating group performance was exceptional, and that our high level of capital investment was a positive sign, reflecting the value in the underlying businesses. We also focused intently upon our operating results to ensure that if an agreement was achieved, our results would help the company emerge in even a better position. We outperformed our projections to emerge in a very strong position.

Q: How did you communicate to the Street during this time to keep them focused on the journey?

Hession: A lot of our communication to the Street was geared toward our anticipated emergence and making sure that the analysts and the key investors continued to be engaged in the company and that they understood it, so that when CEOC did emerge we would not have a significant overhang of having unnatural holders in our shares. Given the amount of dilution we ultimately had as part of the restructuring, we have had some of that overhang, but I think we were able to mitigate it by keeping our shareholder base engaged throughout the process.

Q: As you weathered the storm you were able to make some operational improvements. Can you describe some of those?

Hession: We launched a significant room renovation project, which allowed us to increase growth in RevPAR (revenue per available room) growth and gaming. We also provided our operators with tools to help them better staff their variable labor relative to anticipated demand.

On the technology front, we kicked off an IT renovation cycle that was much more forward-looking. We felt that to be a world-class organization in three to five years we would need to migrate many of our systems to the cloud, and we began that process during the restructuring. We also took a more aggressive approach to deploying technology to aid our marketing efforts, by using Big Data and analytics to better understand customer behavior and direct our marketing investments more effectively. Going back to 2015 we performed targeted reductions to our marketing by hundreds of millions of dollars, which drove a significant change in our ultimate profitability.

Q: Given the cutbacks in marketing, how do you keep customers engaged with the company?

Hession: To put our marketing spend in context, at Caesars Entertainment we spend about $1.9 billion a year on marketing, and another $300 to $400 million distributing that marketing, for a total of around $2.3 billion. Our revenues are just shy of $9 billion, so marketing is a sizeable percentage. To attract customers, we advertise via billboards, TV spots, and, predominantly, through email and direct mail. We also are investing heavily in our app because we believe it increases customer engagement and allows us to market much more effectively. Last year we hit the one-million-download mark, and the dollar volume of transactions flowing through the app is growing significantly every quarter.

Q: When you became CFO of Caesars you brought 13 years of experience in the gaming industry. What are some of the notable changes you've seen over that period?

Hession: The gaming industry has evolved, from being very fragmented, with lots of small operators, to much larger companies that were formed largely through corporate rollups. As a result, the sophistication of the industry has improved across the board, from IT to operations to analytics. Along with that the finance function has had to change significantly, driven mostly by technology. Our finance department used to be much more of a reporting function, providing data and information to frontline operators to help them make decisions, but in the context of "Here's some information; make decisions as you see fit."

Now, because of the complexity of those decisions, the amount of data we have, and the experience we've gained by having 35 U.S. properties that can share leading practices, the finance department plays much more of an advisory role, using centralized information to help operations improve the financial results of the company in many different ways. That role leads to totally different discussions with management and the board about how to prioritize our capital spending. Those are very interesting, fun discussions, versus constantly trying to figure out how to refinance debt, so that's a big and welcome change.

Q: Aside from your growth plans, what other issues are top of mind as you look ahead?

Hession: We are in the entertainment business, which means we have to keep our product fresh and exciting. The industry, broadly defined, is evolving very quickly: apps, e-sports, and many other activities that people enjoy are a form of entertainment. One of the things we are working on is called the "Casino of the Future," a technology-based platform that will allow consumers to connect with friends and peers when they enter our property, as a way to enhance their experience and their enjoyment of the product, and includes other elements that are typically found on social gaming sites.

We also think carefully about younger consumers. Contrary to current wisdom millennials are very willing to pay more money for certain things, but those need to be experiential and high-quality. As a result, when we think about investing in our businesses at Caesars Entertainment, we know we need to provide an environment in which they feel they are getting a differentiated, custom, and unique experience. That approach not only appeals to millennials but to other age groups — it's just that millennials require it.

Finally, we were very pleased by the recent Supreme Court decision to allow states to regulate sports betting. As casino and entertainment providers, we believe that we are very well positioned to benefit as certain states legalize sports betting.

Leading With Resiliency: Lessons From Seven Leaders

Some of the most sought-after business insights are also the most fundamental: Keep things in perspective, be transparent, and understand who you are. Regardless of how simple the elements of good leadership may sound, putting them into practice can be challenging, even for established leaders.

Deloitte's "Resilient podcast series" explores leadership issues in interviews with more than 20 CEOs, senior business executives, and other top leaders representing a wide range of industries. While the leaders shared their diverse personal stories on successfully navigating risk, crisis, and disruption, the discussions also covered what it takes to be a resilient leader.

Following are lessons learned culled from the podcast interviews that provide insights into how seven resilient leaders address disruption and risk.

Keep Things in Perspective

As former supreme allied commander of the North Atlantic Treaty Organization (NATO), Admiral James Stavridis led an intergovernmental military alliance among 29 North American and European countries. While representing the interests of all member states—and through high-stakes operations, such as enforcing a no-fly zone in Libya — Admiral Stavridis learned the importance of humility as a source of resilience.

"Don't over-invest in your self-importance or your legacy," he commented, emphasizing respect for others, regardless of where they are on the org chart. "Remain humble. And I think that allows resiliency."

Stay Focused

Keith Wandell joined Harley-Davidson as CEO during a time when productivity at the motorcycle company was down, competitors were gathering steam, and Harley's network of 1,600 independent dealers was struggling to attract new customers. The former CEO says resilience involved zeroing-in on key priorities that would make the most difference — including revising manufacturing processes and making Harley a more welcoming brand to new demographics and first-time buyers. "Have a clear vision, a clear focus," he explained, adding that resilience requires keeping that focus on the future, not the past. "Don't sit around and brood over what might have been."

Be Transparent

As former senior vice president of corporate governance at the security systems company, Tyco International, Eric Pillmore says resilience came from transparency and the resolve to investigate root causes when the CEO and CFO were found to have stolen hundreds of millions in company assets. "I think human nature tells us 'don't look there.' But I think...get to the bottom of [it] as quickly as possible," said Pillmore. He explained that such transparency is key to resilience, in that it helps leaders get over what happened in the past and focus on moving forward. "Leave no stone unturned."

Be Optimistic

Former Krispy Kreme CEO Daryl Brewster used a similar analogy in discussing his own transparency efforts after a financial controversy. "We'd be turning over some rock, there'd be some other new issue that would come up," he said. Amid such fact-finding, or other depressing news, Brewster pointed out resilience involves retaining a degree of optimism. "It was good to get those issues out," he said. "But it was unproductive just to labor and stew on them." At one point in the crisis, Brewster moved the office of an optimistic, problem-solving manager to be in closer proximity to some colleagues who were getting stressed and overwhelmed. "He brought just a wonderful sense of optimism. Good ole 'got to get it done and let's figure this stuff out,'" Brewster noted, describing the employee's positive attitude.

Innovate and Evolve

In the words of Beth Comstock, former vice chair of GE, we are living in a time of "digital reckoning." Today's leaders must adapt to embrace the shift to digitization, digitizing not only what they work with but how they work. "Only now in business are we are thinking much more systemically because of the digitization and the platform theories, and future leaders will put data at the forefront and own the entire customer journey, both the digital and physical. It's all about the system," she notes.

An advocate of lifelong learning, Comstock has a "10 percent rule" whereby she dedicates 10 percent of her time to discovery. "If there's one thing I feel like I have learned in my career … everyone has to make room to discover what's new and what's next before it hits you in the face or disrupts your business."

Get Back Up

Asked how he helped his newspaper survive disruption as more people turned to online sources, Dallas Morning News Publisher and CEO Jim Moroney didn't hesitate. "My resiliency comes in two parts: I feel like I have a group of people that I can't let down…and we have a mission," he noted, referring to the organization's commitment to quality journalism. He added that a shared sense of mission among a dedicated team helped drive a successful digital transformation that bolstered online news platforms alongside the print edition. Even amid setbacks, Moroney said, "I feel a real sense of responsibility…so that keeps me getting back off the mat every day."

Understand Who You Are

Former Deloitte Global CEO Barry Salzberg made countless decisions over his nearly four decades at the organization. Many of those were mission-critical and had to be made quickly and under great pressure. To keep from getting stuck on tough decisions and to stay resilient, Salzberg developed a clear sense of self and an enduring set of values. "You don't want to sit down and then say, 'Well, who am I and how should I go about making this decision," he explained. "You want to just make the decision…knowing that it is founded on a set of values that will serve you well over time."

Moving Forward

Whether it's a value-destroying crisis, a shift in industry dynamics, or a high-stakes investment in the future, uncertainty comes in many shapes, sizes, and impacts. Many executives know that their ability to effectively navigate risk, crisis, and disruption will likely determine their ability to evolve as a business leader and be successful over time. Resilient leaders embrace important qualities — including determination, transparency, self-awareness, and optimism. They take risk management a step further and ask themselves, "What am I doing today to prepare not only for tomorrow's threats but also tomorrow's opportunities?"

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