Deloitte CFO Signals Survey Report

Q4 2018

February 14, 2019

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About Deloitte CFO Signals

Deloitte CFO Signals is a survey conducted globally at regular intervals by Deloitte to find out what is on the minds of Chief Financial Officers (CFOs). After every survey, the answers of CFOs are compiled and analyzed by Deloitte's experts and published as "Signals" from CFOs. The survey consists of a survey on the economic environment, which is used globally every time, and a topical survey, whose content differs by country.
The first survey in Japan was taken in August 2015, and we are now reporting on its 14th edition. Regarding the survey on the economic environment, we analyze chronological changes in CFOs' thinking as well as their latest forecasts at the time of the survey. In addition to the recurring questions, this time we also asked macro-level questions on the Japanese economy and possible risk scenarios affecting the world's major countries.
As for Japan-specific topics, we chose to ask CFOs about issues related to Survey on the roles of the CFO and finance and accounting departments, and on the sufficiency of personnel in organizations. This edition of the survey was conducted between December 2018 and January 2019, and received responses from 32 CFOs.
Thank you for your cooperation.

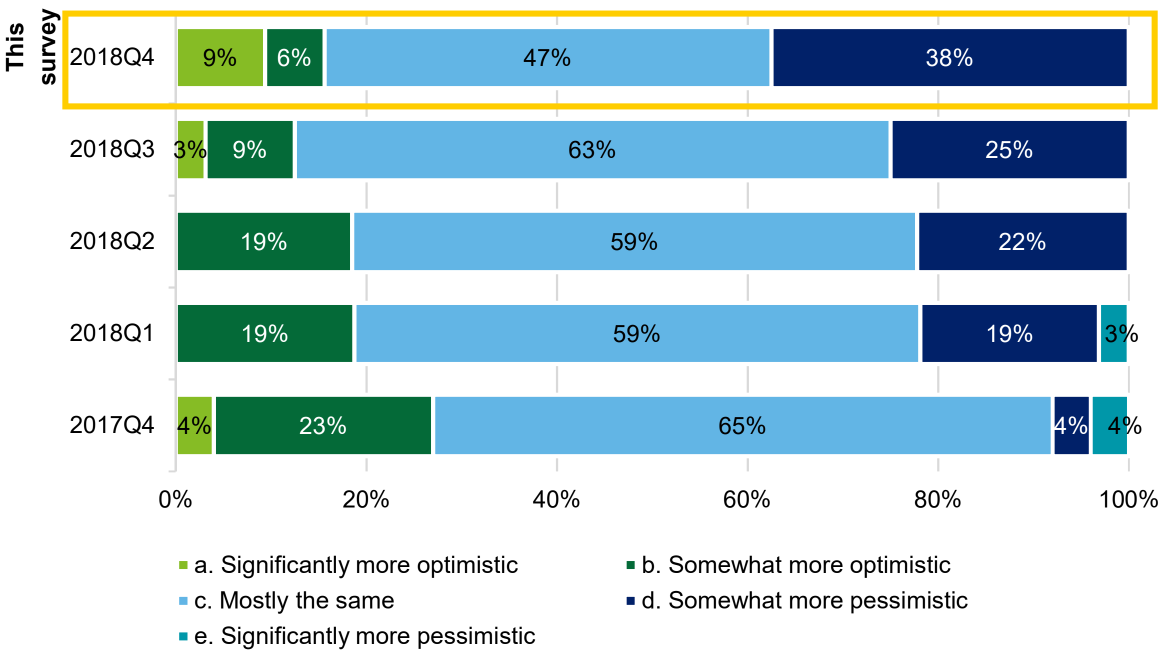
Deloitte Tohmatsu CFO Program
February 14, 2019

Survey on the economic environment

Financial environment prospects

The number of pessimistic responses on financial environment prospects increased for the third consecutive quarter

Graph 1
Compared to three months ago, how do you feel about the financial prospects for your company? Choose the most appropriate answer.

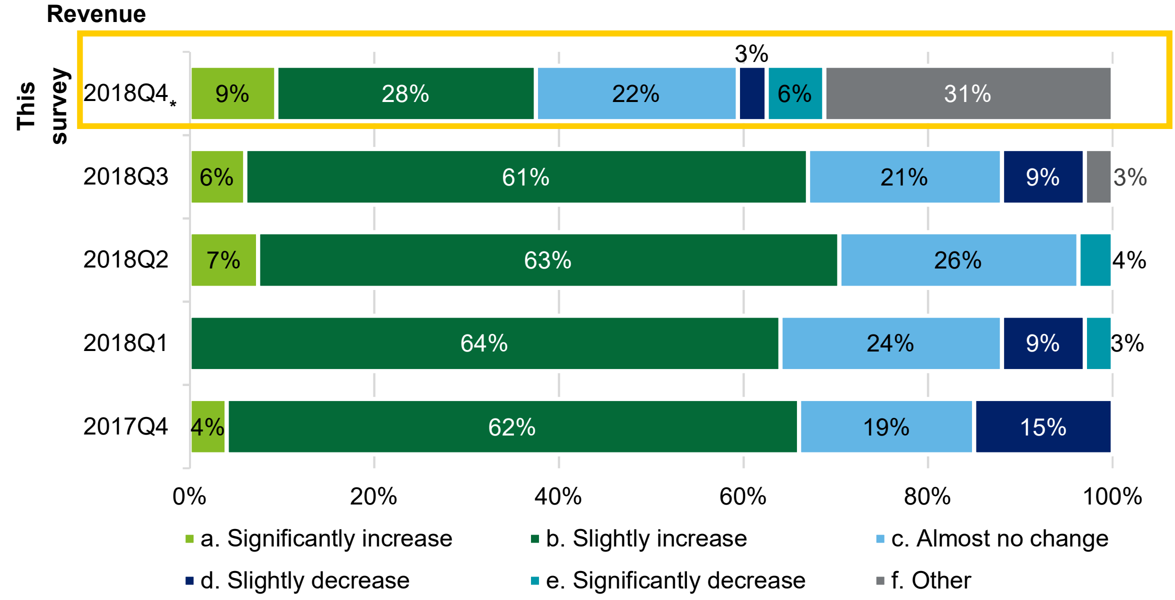


Graph 1 shows how the financial prospects of the respondents' businesses have changed over the last three months. Responses of a, "Significantly more optimistic" or b, "Somewhat more optimistic" in comparison to the previous quarter totaled 15%, marking a slight increase from 12% in the previous survey (Q3 2018). However, the percentage of respondents who chose d, "Somewhat more pessimistic" rose significantly, to 38% from 25% last time, indicating that the CFOs' financial outlook is leaning in a pessimistic direction. Q4 2018, the period covered by this survey, saw a further increase in global uncertainty. In November, the midterm congressional elections in the United States resulted in the ruling Republican Party losing its majority in the House of Representatives. While the leaders of the US and China agreed to hold off on additional tariffs and sanctions at their meeting in November, the direction of US-China trade negotiations going forward remained unclear. The UK parliamentary vote on an agreement between the United Kingdom and the European Union concerning the terms of the UK's exit from the EU, initially set for December, was delayed until January, heightening the risk of a "no-deal" Brexit. The slowdown of the Chinese economy also became even clearer, while financial markets experienced a continued drop in stock prices at the end of the year. The resulting growth in global uncertainty, which affected both the real economy and financial markets, can be seen to have reduced CFO optimism concerning financial prospects. As discussed later in this report, the slowdown of the Chinese economy can be considered a particularly significant factor behind the worsening financial outlook. This is because said slowdown is beginning to actualize itself in the form of worsening corporate performance. The CFOs' views on financial prospects are expected to remain exposed to downside risk going forward.

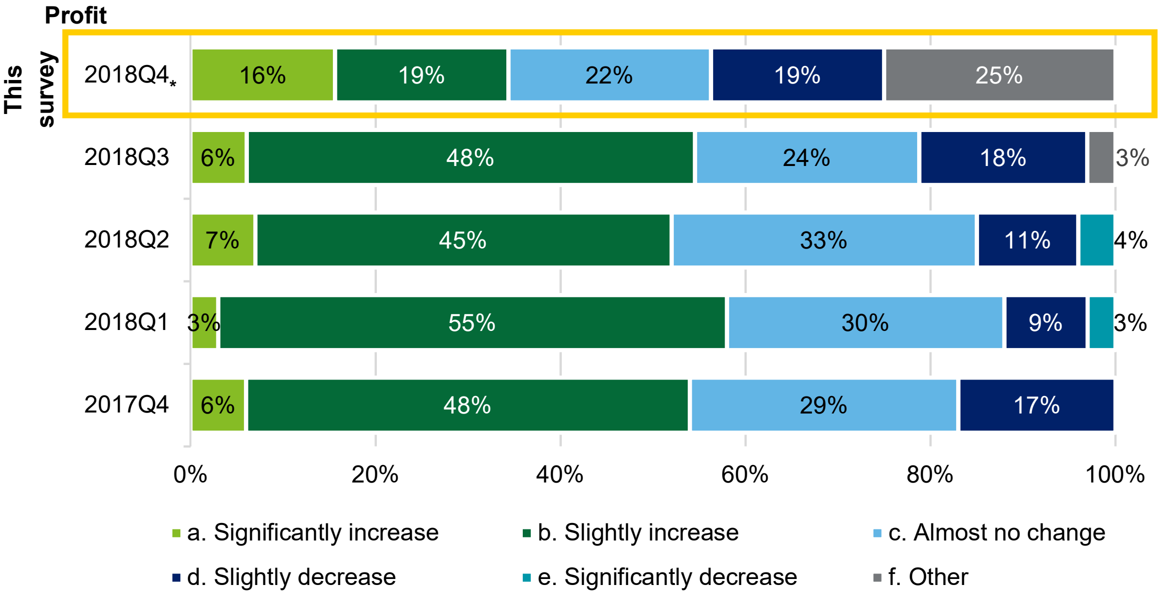
Business performance outlook

The business performance outlook worsened significantly

Graph 2
How do you expect your key operating metrics to change over the next 12 months? Choose the most appropriate answer.



*The number of blank responses and multiple responses increased



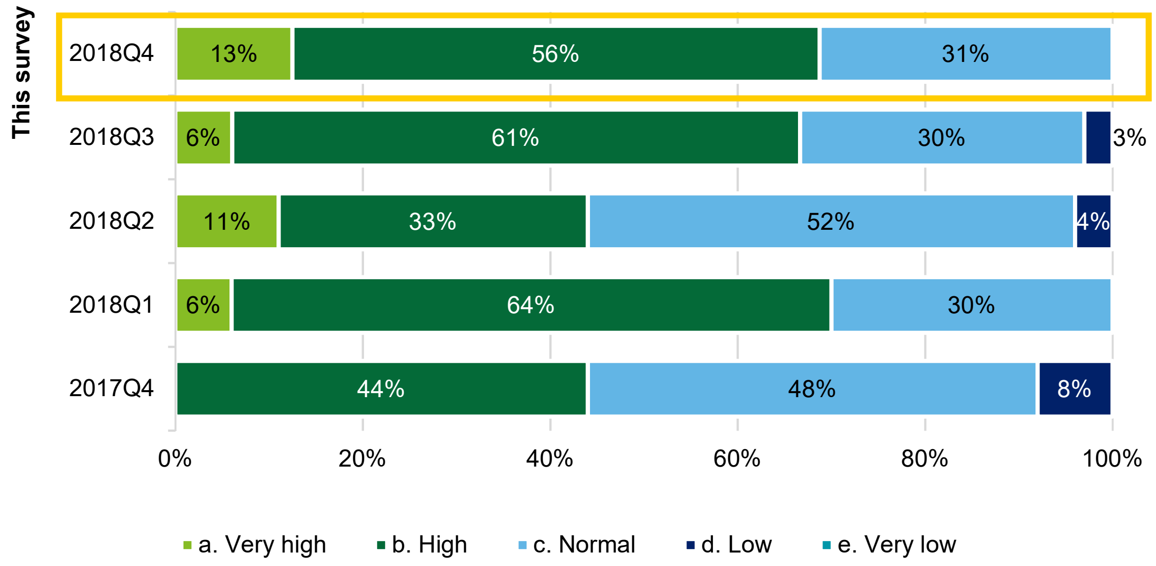
*The number of blank responses and multiple responses increased

Graph 2 shows CFOs' outlook for their company's financial performance (revenue and profit) over the coming year. A total of 37% expected revenue to either a, "Significantly increase” or b, “Slightly increase,” which marks a dramatic decrease from the 67% in the previous survey. At the same time, a total of 35% expected profits to a, “Significantly increase” or b, “Slightly increase”—also a significant drop from the 54% in the previous survey. In Q4, a growing sense of uncertainty in the global economy, the more pronounced slowdown of the Chinese economy, and a worsening situation in the financial markets combined to make explicit a negative tendency in the business performance outlook of CFOs. In fact, the financial results released by some American companies in January showed decreases in revenue, which were attributed to the slowdown in China. Changes in the global economy, and especially weaker growth in China, are starting to have noticeable impact in the form of lower corporate revenue. In addition, in the past two quarters we have seen an increase in the number of multiple or blank responses in relation to business performance outlook. This trend appears to reflect growing uncertainty in the business environment, which we will take a closer look at later. Downside risk factors in 2019 include predicted weaker growth not only in China but throughout the global economy, as well as a potential “no-deal” Brexit and ongoing trade friction. The business performance outlook of companies can thus also be said to be exposed to downside risk.

Uncertainty

Uncertainty increased further

Graph 3
How would you rate the level of financial and economic uncertainty faced by your business? Choose the most appropriate answer.

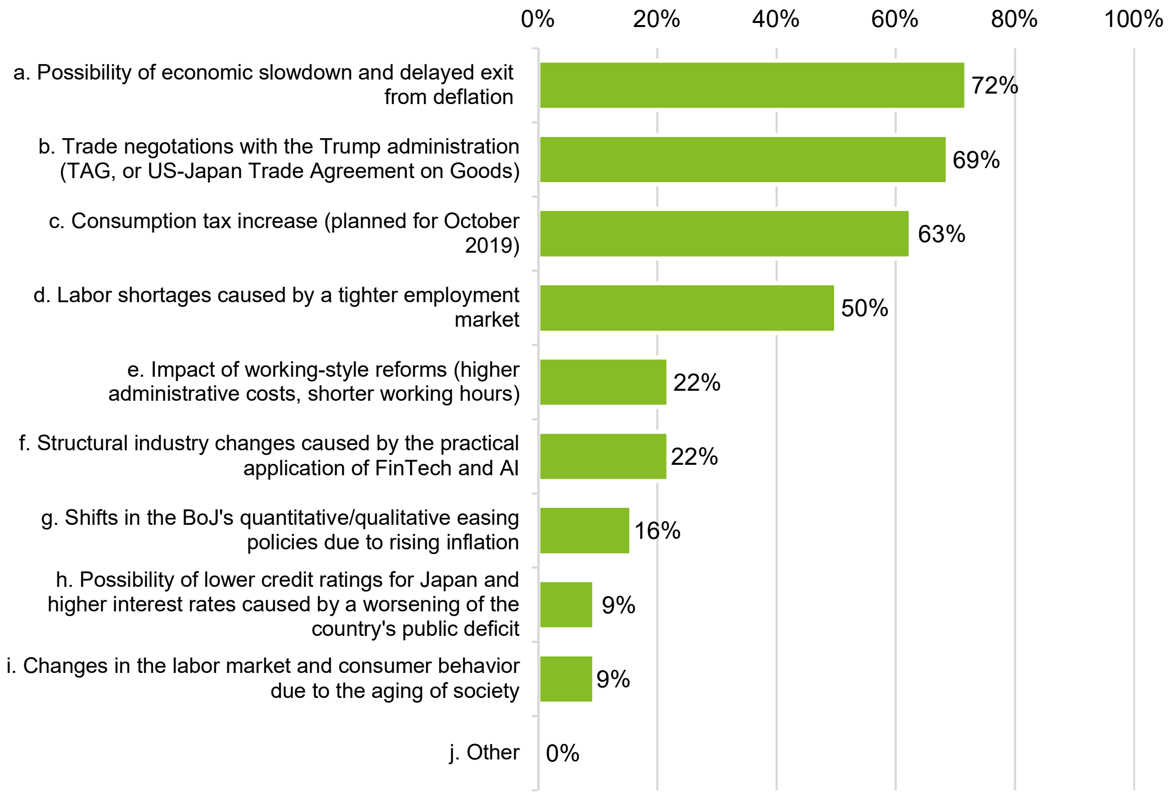


Graph 3 shows CFOs' perception of financial and economic uncertainty. A total of 69% of respondents said that uncertainty was "very high" or "high"—a further increase from 67% in the previous survey, indicating that uncertainty remains high. As mentioned in Graph 1, possible background factors for this uncertainty include the unclear direction of trade friction between the US and China, the heightened risk of the UK leaving the EU without a deal, concerns about the slowdown of the Chinese economy, and falling stock prices. Many of these uncertainty factors, such as predicted weaker growth in both China and throughout the global economy, a "no-deal" Brexit, and trade friction, remain in 2019. In addition, as Europe is seeing populist forces strengthen their presence in the run-up to the European Parliament elections in May, factors such as German Chancellor Angela Merkel's resignation as head of the ruling CDU party and policy reversals in France caused by growing demonstrations, resulting in a predicted expansion of that country's budget deficit, contribute to a sense of political instability. Political uncertainty is also on the rise in the United States, exemplified by events such as the prolonged government shutdown from December, the ongoing Russia investigation, and the withdrawal of the US military from Syria. Uncertainty in the business environment of companies appears set to remain high in 2019.

Key change factors in the Japanese economy

Increased focus on deflation and slower growth

Graph 4
For the items below, please choose up to four possible changes affecting the Japanese economy that you believe need particular attention based on their likelihood and expected impact on business



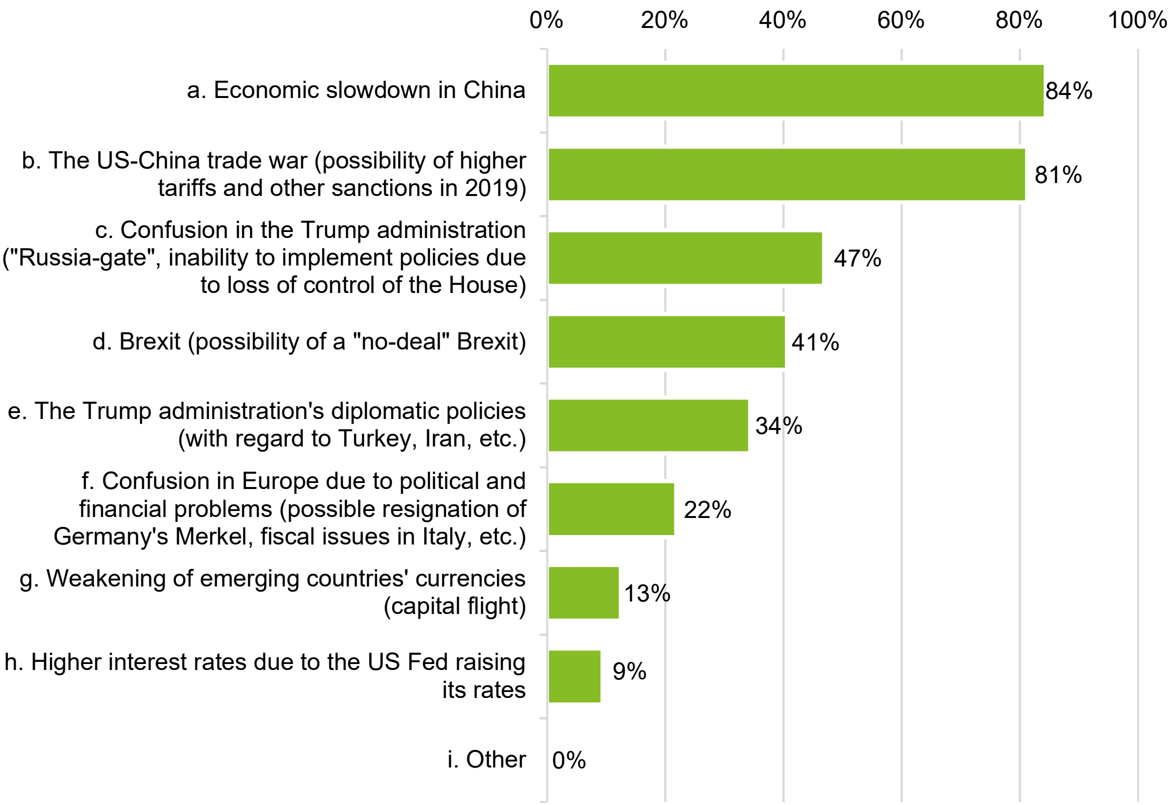
Graph 4 shows what trends in the Japanese economy are most closely watched by CFOs when planning business development over the next one-year period.
This time saw a, “Possibility of economic slowdown and delayed exit from deflation” make a swift jump, rising from the seventh most popular response in the previous survey to number one this time. The Japanese economy contracted in Q3 due to the impact of natural disasters, but was expected to bounce back to growth in Q4. That concerns about an economic slowdown and deflation grew despite this can be attributed to factors such as worries about what impact weaker growth both in China and globally will have on the Japanese economy, and concerns about slower inflation due to the drop in oil prices seen in Q4. The second most popular answer was b, “Trade negotiations with the Trump administration (TAG, or US-Japan Trade Agreement on Goods),” which we added for this edition of the survey. With a breakthrough yet to be achieved in the trade negotiations between the US and China, CFOs appear to be expecting the US to take a hardline stance in negotiations with Japan as well, and are paying close attention to the impact the implementation of auto tariffs would have. Coming in third place was c, “Consumption tax increase (planned for October 2019),” which was the top answer last time. CFOs appear to have assumed the view that the impact of a consumption tax hike in October on

consumption and other indicators would be limited by fiscal stimulus measures and the implementation of a reduced tax rate on certain items. Furthermore, d, “Labor shortages caused by a tighter employment market” and e, “Impact of working-style reforms,” which have been among the most popular responses in the past, seem to be losing out to other concerns. The rise in economic uncertainty appears to be prodding CFOs to switch their focus from internal cost structures to external economic factors that have a direct impact on business performance.

Key change factors in the global economy

Most attention is being paid to slowing growth in China

Graph 5
From the items below, choose up to four events that risk affecting foreign economies and that you believe need particular attention, based on their likelihood and expected impact on business



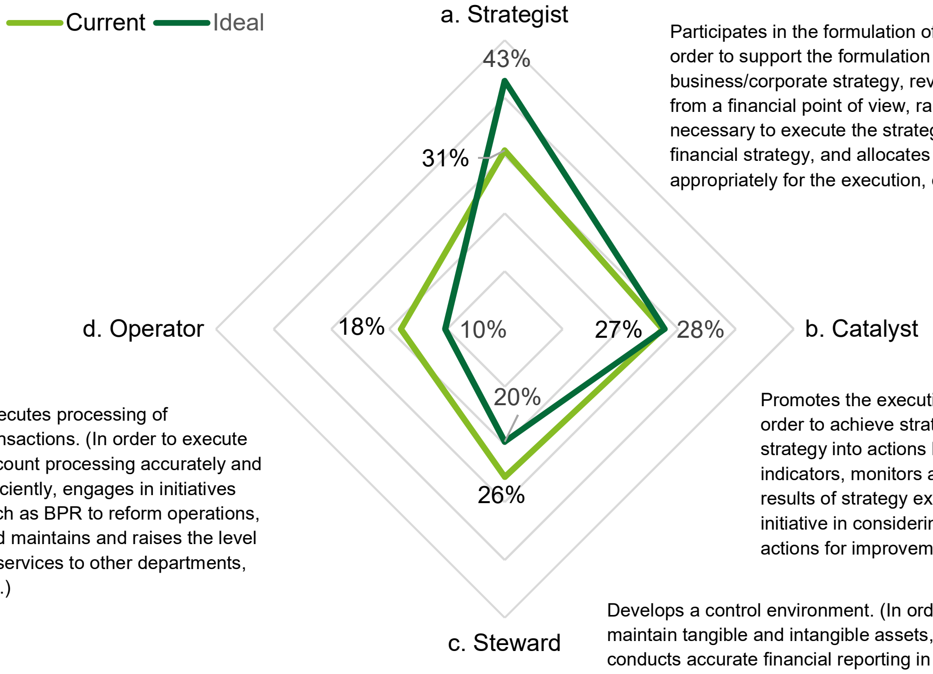
Graph 5 shows what trends in the global economy are most closely watched by CFOs when planning business development over the next one-year period. Risk events related to China occupied the two top spots, with a, “Economic slowdown in China” coming in first and b, “The US-China trade war” in second. In 2018, the Chinese economy grew at a rate of 6.6% year-on-year, which is its slowest pace in 28 years. This slowdown is expected to continue in 2019, with annual growth forecast to end up between 6.0 and 6.5%. Weaker consumer spending is particularly notable in China, and while the government is examining measures such as large tax cuts and looser credit, their viability and effects are unknown at this point. The US-China trade war is also bringing about the prospect of further downside risk concerning China. The slowdown in China is already beginning to have a clear negative impact on non-Japanese companies’ performance, as weaker smartphone and other sales are taking their toll. The CFOs’ focus on the Chinese economy as a factor directly connected to business performance has increased in comparison to past surveys. The third most popular response was c, “Confusion in the Trump administration,” which ranked fifth in the previous survey. The United States went through a prolonged government shutdown, caused by disagreement between President Trump and Congress on the issue of building a wall on the border with Mexico, while the investigation into the “Russia-gate” scandal appears to be nearing its conclusion. President Trump’s diplomatic stance has also hardened after his Republican Party lost control of the lower house of Congress in the midterm elections in November. At any rate, trends in the Chinese economy with a direct impact on Japanese companies appear set to remain closely watched by CFOs.

Survey on the roles of the CFO and finance and accounting departments, and on the sufficiency of personnel in organizations

Roles of the CFO and time allocation

CFOs appear willing to make a further shift from a “defensive” role into an “offensive” one

Graph 6
Regarding the 4 roles below, please write your current time allocation and your ideal time allocation as CFO (Please answer in percentages that add up to 100%).



Participates in the formulation of strategy. (In order to support the formulation of business/corporate strategy, reviews strategy from a financial point of view, raises funds necessary to execute the strategy, formulates financial strategy, and allocates resources appropriately for the execution, etc.)

Promotes the execution of strategy. (In order to achieve strategic goals, turns strategy into actions based on targets and indicators, monitors and analyzes the results of strategy execution, and takes the initiative in considering and executing actions for improvement, etc.)

Develops a control environment. (In order to protect and maintain tangible and intangible assets, sets rules, conducts accurate financial reporting in a timely manner, and maintains relationships with external stakeholders, etc.)

Executes processing of transactions. (In order to execute account processing accurately and efficiently, engages in initiatives such as BPR to reform operations, and maintains and raises the level of services to other departments, etc.)

First, we asked the CFOs about their current and ideal time allocation regarding the four roles. The results show that CFOs currently allocate 31% of their time to being a strategist, which takes up more time than any of the other three roles. This suggests that CFOs are able to contribute to the development of strategy as members of upper management. However, the fact that the respondents would ideally allocate 43%, or almost half, of their time to being a strategist suggests that strategy-related expectations for CFOs have been rising further in recent years. On the other hand, CFOs are currently spending the least time, or 18%, on playing the role of operator, but would like to reduce the time allocated to such tasks even further to about 10%.

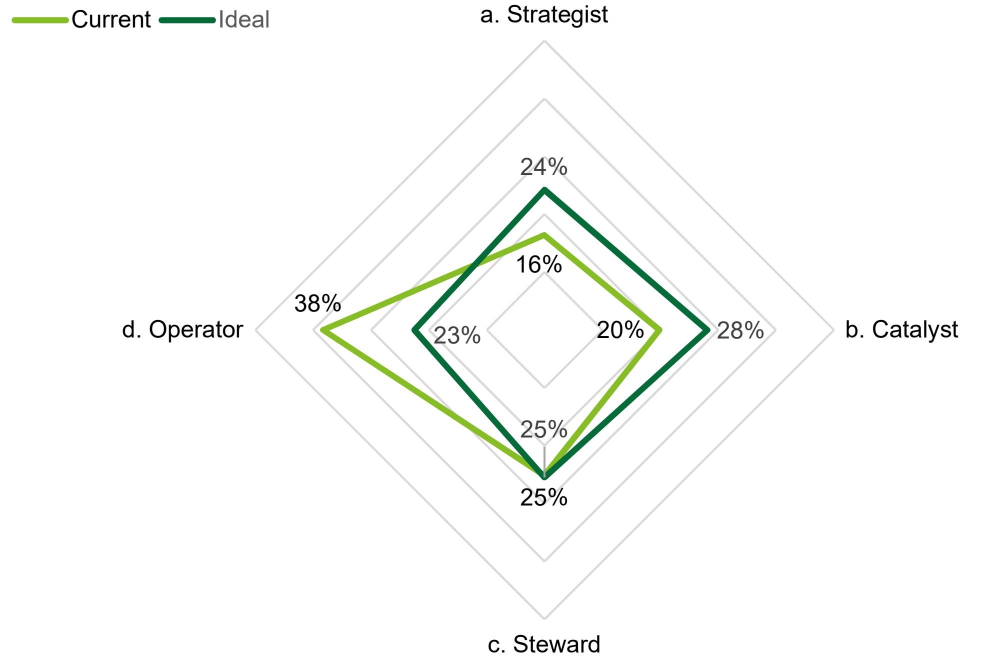
Based on the above, we can say that instead of emphasizing a balance between the four roles, CFOs would like to further decrease the time they spend on “defensive” roles, which are those of steward and operator, and are hoping to devote themselves to developing and promoting the execution of strategy by allocating more time to playing the “offensive” roles of strategist and catalyst.

Roles and time allocation of finance and accounting departments as a whole

CFOs think it would be preferable for finance and accounting departments as a whole to allocate time evenly among the four roles

Graph 7

Regarding the 4 roles below, please write the current time allocation (allocation of resources) and ideal time allocation (allocation of resources) of the entire finance and accounting departments. (Please answer in percentages that add up to 100%).



Next, we asked about the current and ideal time allocation regarding the four roles in finance and accounting departments on a whole. Most time, or 38%, is currently allocated to the role of operator, clearly exceeding the ideal allocation. On the other hand, the "offensive" roles of strategist and catalyst currently both receive 8% less time than in the ideal scenario, suggesting that the current situation at companies necessitates spending more time on operational tasks than would be preferable.

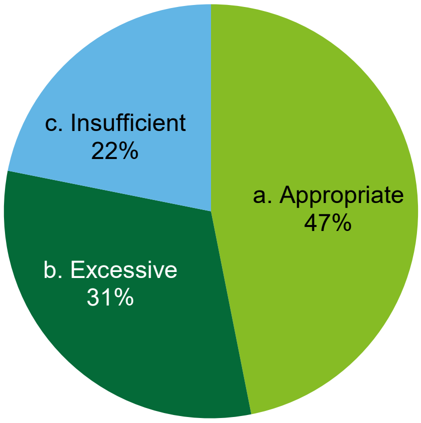
Unlike in the case of the CFOs themselves described above, the results for finance and accounting departments as a whole suggest that the respondents find it preferable to allocate time evenly across the four roles. How to reduce the time spent on the operator role and balance out time evenly among the roles is likely to be raised as an issue from here on.

The number of personnel in finance and accounting departments

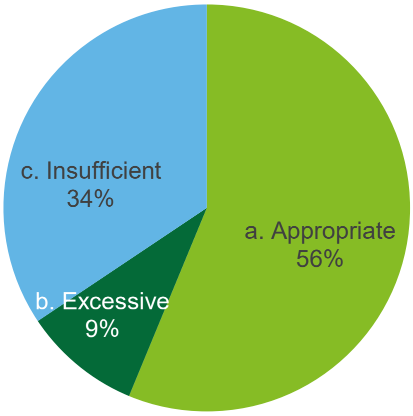
About half of all respondents said that the numbers of management personnel (managers and section chiefs) and staff are appropriate

Graph 8
For your perceived roles of finance and accounting departments, what is your opinion on the current number of personnel in finance and accounting departments in your group as a whole?

8.1 How do you find the current number of management personnel (managers and section chiefs)?



8.2 How do you find the current number of staff members?



Lastly, we asked the CFOs to give their opinions on the current numbers of management personnel (managers and section chiefs) and staff in their companies' finance and accounting departments. The results show that about half of the participating companies find their numbers of both management personnel and staff appropriate. However, the second most popular answers reveal differences. Regarding the number of staff members, the answer chosen by the second largest number of respondents was c, "Insufficient" (34%). The reasons for this can be thought to include that finance and accounting departments, which are indirect departments, are ever only assigned a limited number of young personnel, and that maintaining and training allocated talent is not conducted as planned. As securing talent is expected to remain a challenge, how to secure and retain talented personnel can be considered one of the most important issues for finance and accounting organizations.

On the other hand, the second most popular answer concerning the number of management personnel was b, “Excessive” (31%). While existing personnel structures are a significant factor here, at a time when organizations as a whole have limited resources to work with, there appears to be an overabundance of managers with experience of finance and accounting. It is somewhat bothersome if CFOs are finding it difficult to come up with assignments and career paths for such individuals on a daily basis. Making effective use of all members of finance and accounting departments by utilizing models for future careers and measures for achieving these (such as career paths and training), all while taking into account the balance between managers and staff in the personnel structure, can be considered essential for the evolution of finance and accounting organizations.

As of late, organizations and systems are being revised as a result of various initiatives, including efforts to reform working styles. The personnel structures of finance and accounting departments are also being slimmed down. Thinking about how to conduct operations without wasting limited resources can be expected to lead to the achievement of ideal time (resource) allocation for both CFOs and finance and accounting departments as a whole.

What is the CFO Program?

The CFO Program is a comprehensive initiative by Deloitte Tohmatsu Group, aiming to provide support to the CFOs of companies that underpin the Japanese economy, add to the capabilities of those CFOs' organizations, and thus revitalize the Japanese economy itself. Professionals with different specializations work together as trusted advisors to help CFOs solve the problems they face. We also endeavor to improve the competitiveness of Japanese businesses by providing CFOs with the latest information, including global trends, as well as networking opportunities across different companies and industries.

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