

Deloitte CFO Signals Survey Report

2020 Q3

December 2020

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About Deloitte CFO Signals

Deloitte CFO Signals is a quarterly global survey for investigating the thinking and actions of leading Chief Financial Officers (CFOs). We share the highlights of survey results with analysis from Deloitte Tohmatsu and publish them as the CFO Signals report.

The survey consists of two sessions: the “Survey on the Economic Environment”, which is assessed globally in every edition, and “Survey on Hot Topics”, which varies for each country. (None of “Hot Topics” session for this edition.)

In Japan, it was conducted for the first time in August 2015, making this the 22nd edition. In the “Survey on the Economic Environment”, we analyse chronological changes in CFOs’ thinking as well as the latest forecast at the time of the survey. In addition to recurring questions, *we also inquire about* the operational impacts and changing expectations under the increased uncertainty caused by the COVID-19 pandemic

Surveys for this edition were conducted in November 2020, and we were able to receive responses from 40 CFOs and finance and accounting executives.

Thank you for your cooperation.

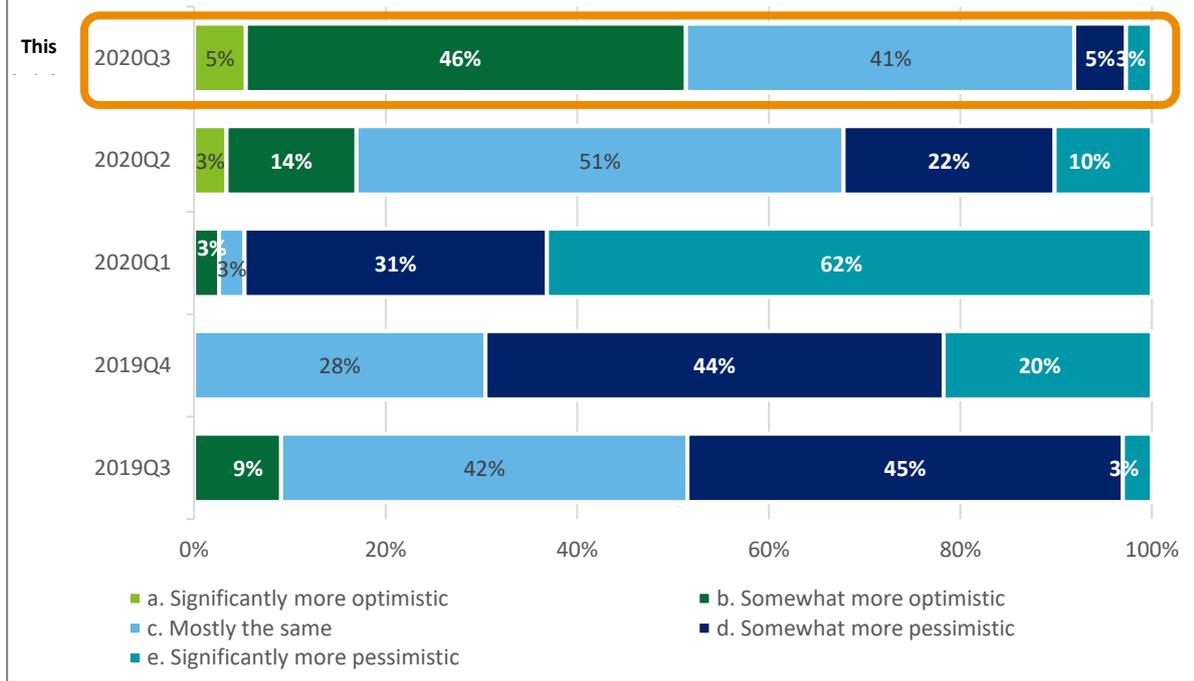
Deloitte Tohmatsu Group
The CFO program
December 2020

Survey on the economic environment

Financial environment prospects

Financial environment outlook has improved significantly, but the situation is uncertain.

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



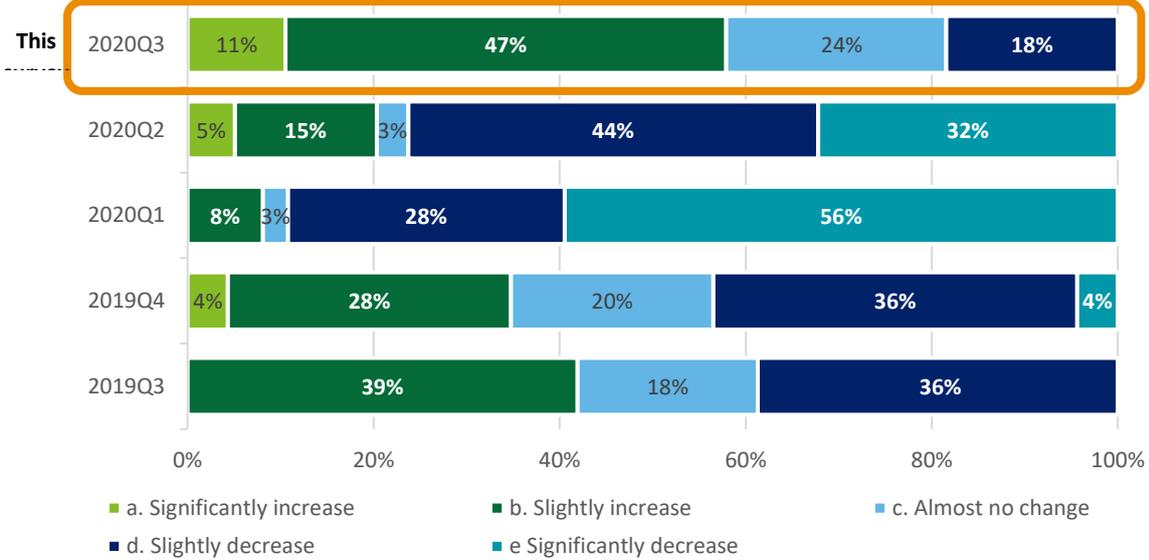
Graph 1 shows how the financial prospects of the respondents’ businesses have changed over the last three months. In this 2020Q3 survey, 51% of CFOs were "significantly more optimistic" or "somewhat more optimistic" about their financial outlook, up sharply from 17% in the previous survey, indicating that the financial outlook has brightened for the majority of CFOs. During the survey period in November, the number of new coronavirus infections was decreasing in major countries and economic activity was recovering. In Japan, the second wave of coronavirus cases had ended. The government's "Go To" campaign had started, and the economy was improving. The Japanese real GDP growth rate in the July-September quarter was 22.9% on an annualized basis, the first growth in four quarters. This economic recovery is considered to have greatly improved CFOs’ business confidence. However, the CFOs’ financial outlook is likely to deteriorate again in the future. Coronavirus infectious increased again around the world, starting around November. In Japan, the number of new infections per day exceeded 2,000 in late November, raising the risk of healthcare system collapse. In some prefectures, restaurants’ business hours were shortened, and the *Go To Travel* campaign was suspended. The spread of the disease is likely to worsen business sentiment during the holiday season.

 **Business performance outlook**

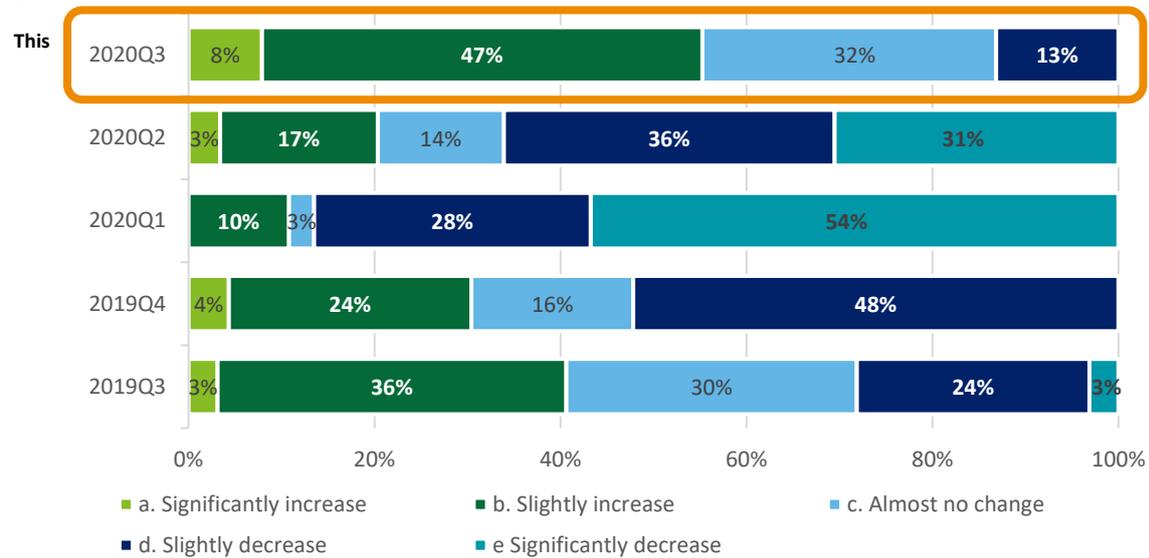
Both revenue and profit are expected to increase.

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

[Revenue]



[Profit]

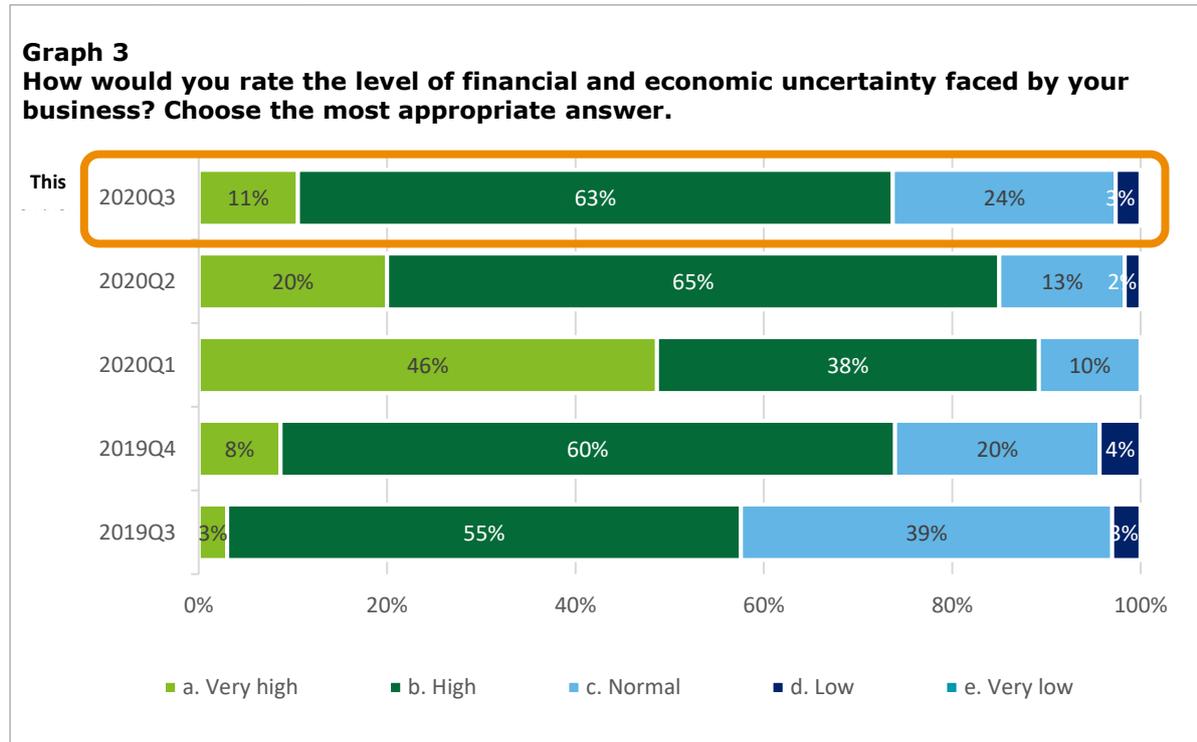


Graph 2 shows CFOs' outlook for their company's financial performance (revenue and profit) over the coming year. As with financial environment prospects, revenue outlook has improved significantly in this 2020 Q3 survey. The total number of respondents who said that they expect business performance to "significantly increase" or "slightly increase" was 58% for revenue and 55% for profit, both sharp increases from the previous survey to over

50%. The temporary decrease in coronavirus infections and the resumption of economic activities have likely improved CFOs' business performance prospects. However, as with the outlook for the financial environment, performance outlook is likely to worsen again in the next survey due to the resurgence in infections and voluntary reduction in economic activity after November. The DI in the Economy Watchers Survey turned downward in November for the first time in three months. The Bank of Japan's Tankan survey in December also showed that the DI for the large non-manufacturing sector's outlook declined from the current level. All of these indicators suggest a possible deterioration in the items covered by the Economy Watchers Survey and among large corporations. However, many companies, especially those that have benefited from the economic environment of the COVID-19 crisis, are developing new business models to adapt to this new normal. As a result, companies' tolerance to the spread of coronavirus infections is likely to be considerably higher than in the early stages of the pandemic. Companies' sensitivity to changes in the number of coronavirus infections in relation to their business sentiment may gradually decline.

 **Uncertainty**

Uncertainty remains high



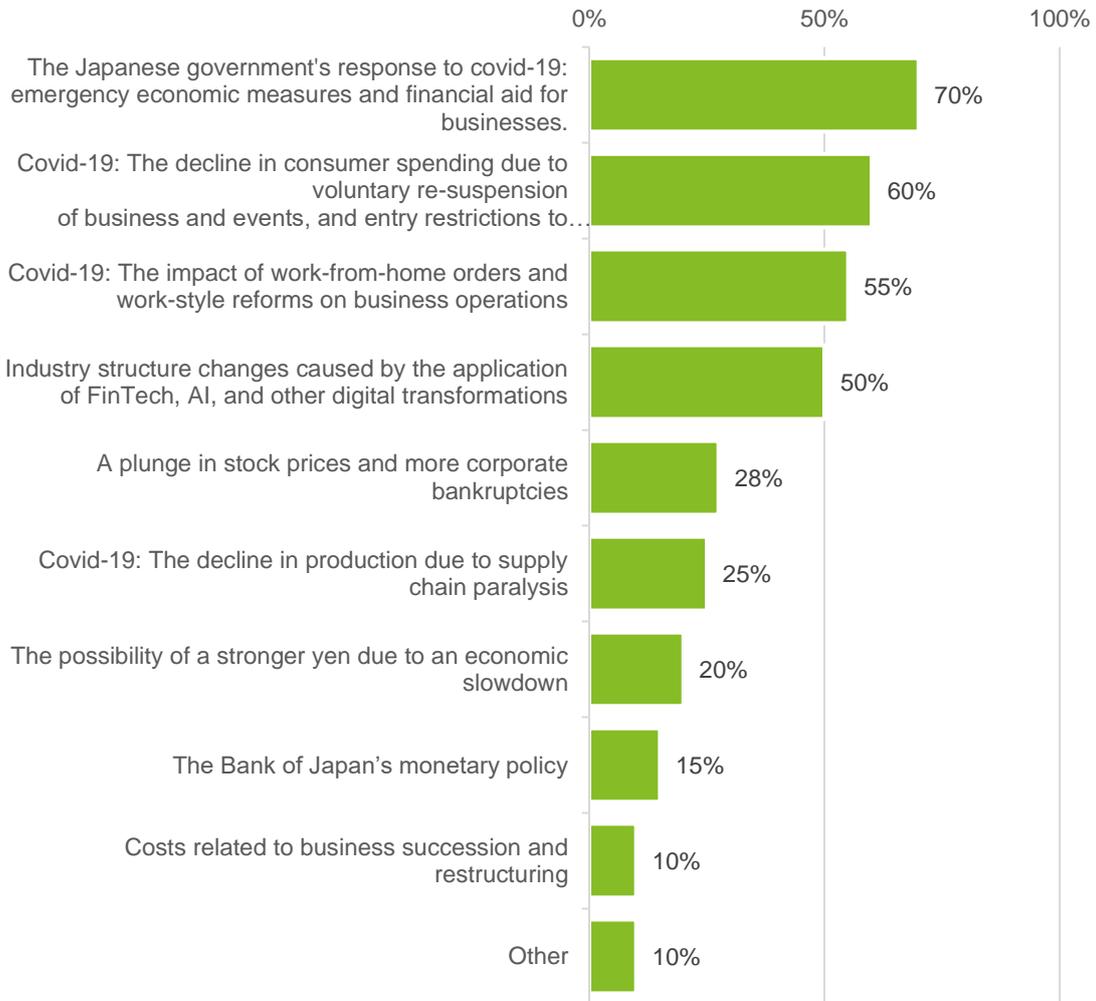
Graph 3 shows CFOs’ perceptions of financial and economic uncertainty. In this 2020 Q3 survey, the total response rate for "very high" and "high" was 74%, a slight decrease from 85% in the previous survey, but still high. Despite improvements in the financial environment and business performance outlooks, it is not certain that this trend will continue in the future. Coronavirus vaccines have been developed, and vaccinations have begun in the UK and the US. However, uncertainty still remains regarding the vaccine’s effectiveness and the possibility of its widespread use in Japan. The high uncertainty in financial and economic conditions suggests that business performance outlook may continue to fluctuate. With high uncertainty regarding companies’ performance, it is unlikely that their capital investment, one element of economic growth, will increase. According to the Bank of Japan's December Tankan survey, the capital investment plans of major corporations were already revised downward to negative year-on-year growth in the middle of fiscal 2020.

Uncertainty is likely to persist for the time being until the covid-19 situation stabilizes.

¥ Key factors in the Japanese economy

The Japanese government's covid-19 response plan is the biggest concern.

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 development prospects over the next one-year period.



- Other additional comments from respondents:**
- Trending toward carbon neutrality
 - Widespread use of coronavirus vaccines
 - Decline in capital investment (overall, not just supply chain disruptions)
 - Rapid increase in unemployment

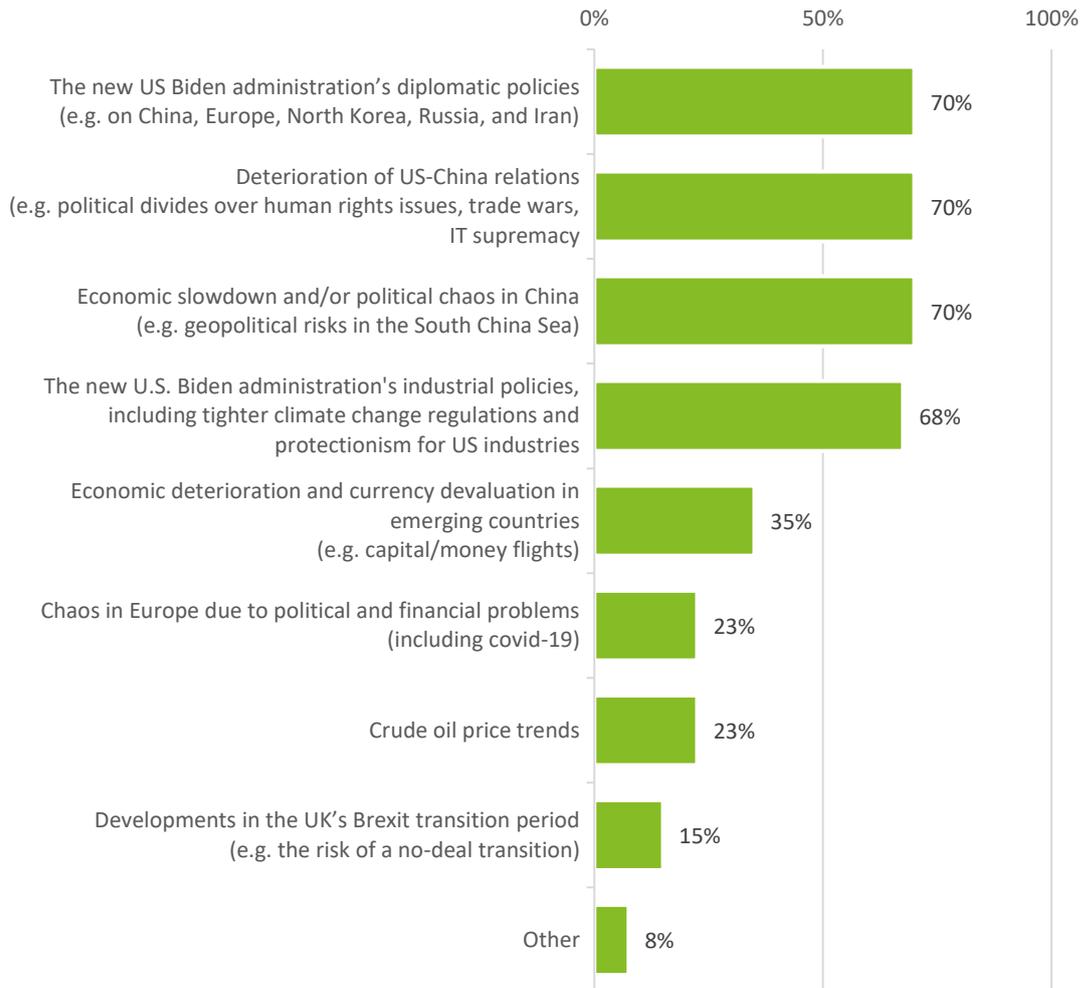
Graph 4 shows what trends in the Japanese economy CFOs will most closely watch when preparing business plans over the next year. In this 2020 Q3 survey, as in the previous 2020 Q2 survey, covid-19 related items ranked high. Number one was "The Japanese government's response to covid-19: emergency economic aid and financial aid for businesses," indicating CFOs' perception that maintaining growth in the Japanese economy still depends on government spending. In second place was the "The decline in consumer

spending due to voluntary re-suspension of business and events, and entry restrictions to Japan," again drawing attention to the trends in consumer spending that support the economy. The third most important factor was "the impact of work-from-home orders and work-style reforms on business operations", indicating that development and adaptation to new business styles post-Corona remains a challenge for companies. Number four was "Industry structure changes caused by the application of FinTech, AI, and other digital transformations". The acceleration of digitalization triggered by the covid-19 crisis, and medium- to long-term changes in industry structure are also important concerns for CFOs. However, the first priority seems to be getting out of the immediate covid-19 crisis.

€ Key factors in the global economy

The biggest concerns are China and the Biden administration in the US.

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 development prospects over the next one-year period.



Other additional comments from respondents:
 -Post-covid recovery of the US economy including the hospitality and travel sectors
 -Delays in the economic recovery of Southeast Asia
 -Climate change policy

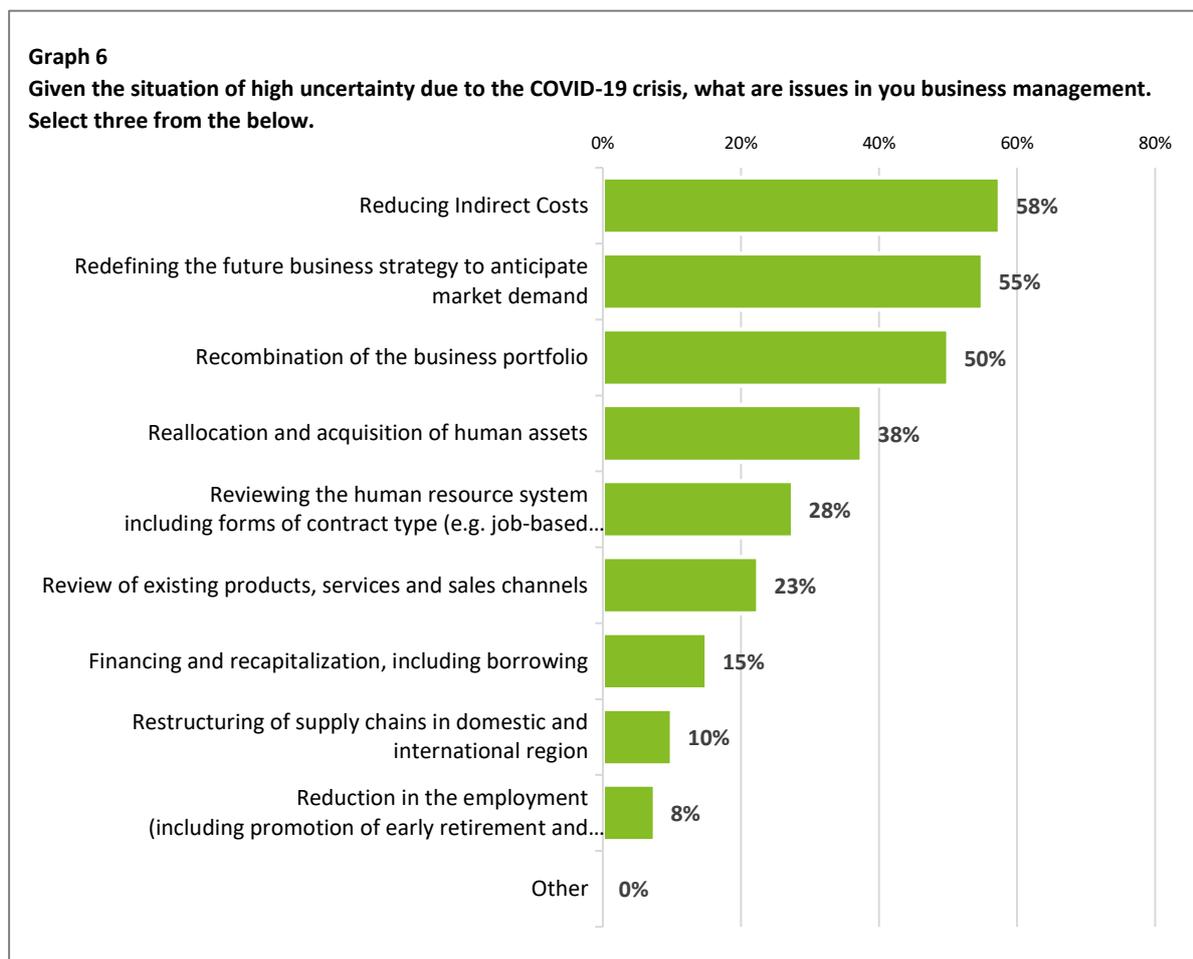
Graph 5 shows what trends in the global economy CFOs will most closely watch when preparing their business plans over the next year. The four options related to the U.S. Biden administration's policies, China's economic trends, and U.S.-China relations were the top choices, all with almost the same response rate of about 70%. The policies of the U.S. Biden administration, which will take office in 2021, are expected to take a significant shift in direction from those of the current Trump administration. Having said that, the Biden

administration will maintain a tough stance on relations with China regarding human rights, national security, and preserving American jobs. On the trade front, however, it is unlikely that the new administration will resort to aggressive measures such as imposing punitive tariffs. China was the first country in the world to recover from the covid-19 crisis, but it was clear even before covid-19 that its economy was on a medium-term slowdown. For Japan, there are major risk scenarios in the future, such as the US's trade and security policies on Japan, and China's geopolitical risks for Japan. It is likely that trends in the U.S. and China will continue to be points of focus for CFOs in the near future.

Survey on the operational impacts and changing expectations under the increased uncertainty caused by the COVID-19 pandemic

Management issues under high uncertainty

In addition to reducing indirect costs, many companies have identified the need to redefine their business strategies and reconfigure their business portfolios as their management issues in the current highly uncertain environment.

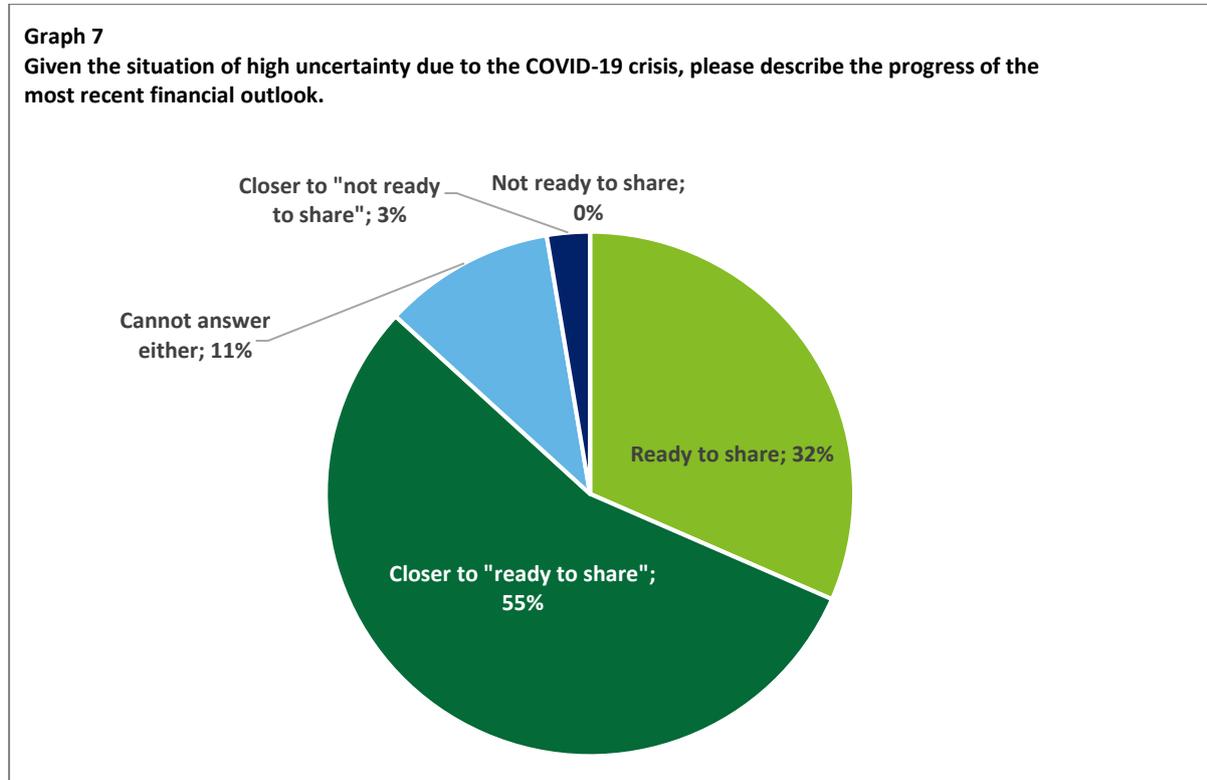


Many companies have taken countermeasures since the continuing COVID-19 pandemic began in early 2020, and their top issue is to reduce indirect costs. This indicates that many companies are trying to secure their profits in these uncertain times by cutting their indirect costs.

This survey also revealed that companies are redefining their business strategies in preparation for a rebound, viewing the current strong economic performance as a sign that demand is recovering faster than expected. Companies are also thinking of recombining their business portfolios to shift their focus from businesses which have no prospect in their demand recovering, to businesses for which growth is expected.

Preparation of financial outlook

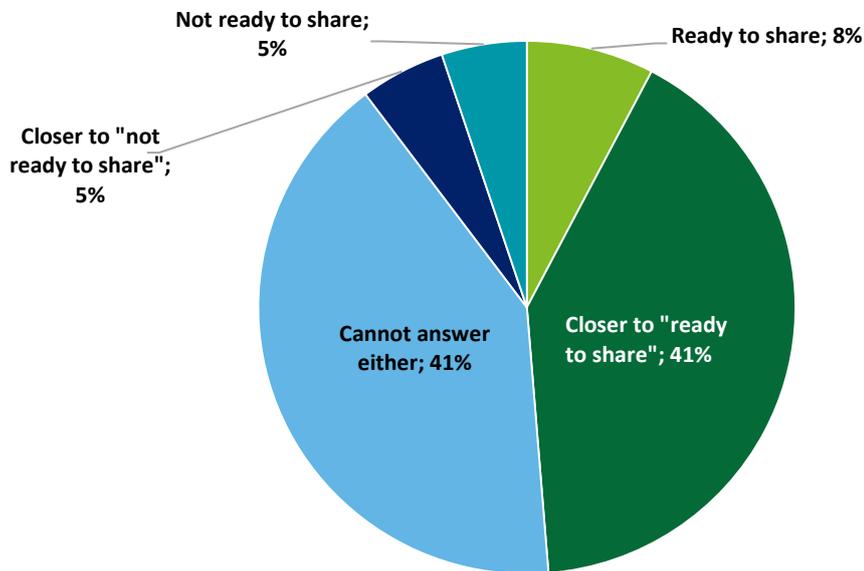
About 90% of the respondents were able to prepare their most recent financial outlooks, and about 50% were able to prepare their medium-term financial outlooks.



With regard to the progress of preparing the latest financial outlook, approximately 90% of companies responded that they are “ready to share” or “closer to ‘ready to share’”. The survey was conducted just prior to the end of the third quarter for companies with a fiscal year ending in March, indicating that most companies have a clear picture of where they stand in the current fiscal year.

Graph 8

Given the situation of high uncertainty due to the COVID-19 crisis, please describe the progress of the *medium-term* financial outlook.

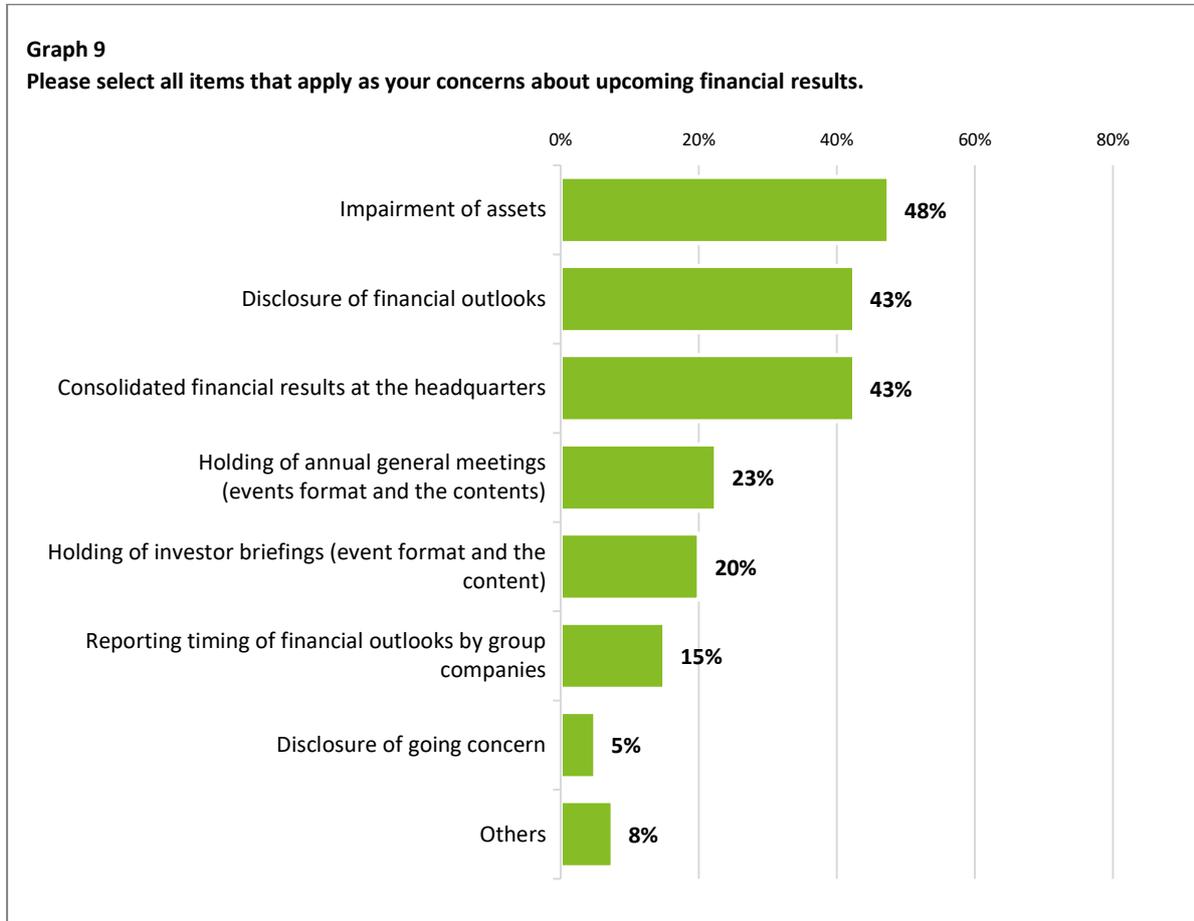


About 50% of companies responded that their medium-term financial outlook is "ready to share" or "close to 'ready to share'". On the other hand, about 40% answered that it was "cannot answer either," indicating that nearly half of the companies surveyed are either not fully aware of possible future changes in the business environment, or feel a strong sense of uncertainty.

In such a severe times, many companies are likely to formulate more simulations compared to normal times in response to changes in the business environment, as well as changes and business operations within those scenarios. Given the results discussed later, it can be inferred that expectations toward the accounting and finance divisions regarding scenario planning for future business prospects are growing.

 **Concerns about upcoming financial results**

Companies are concerned about impairment of assets held, disclosure of financial outlook, and carrying out consolidated closing at the headquarters.



One of the top concerns for this year's financial results is the impairment of assets held. It is recent memory that listed Japanese companies reported large impairment losses for FY 20 March, and this concern continues for FY 21 March. This is because some companies and businesses have not recorded any impairment losses in their FY 20 March financial results, claiming that they could not reasonably estimate the impact of COVID-19 and that their future business prospects were uncertain. The survey results shown in Graphs 7 and 8 suggest that companies have begun to finalize their financial outlooks, so impairment of assets held is a concern for this fiscal year.

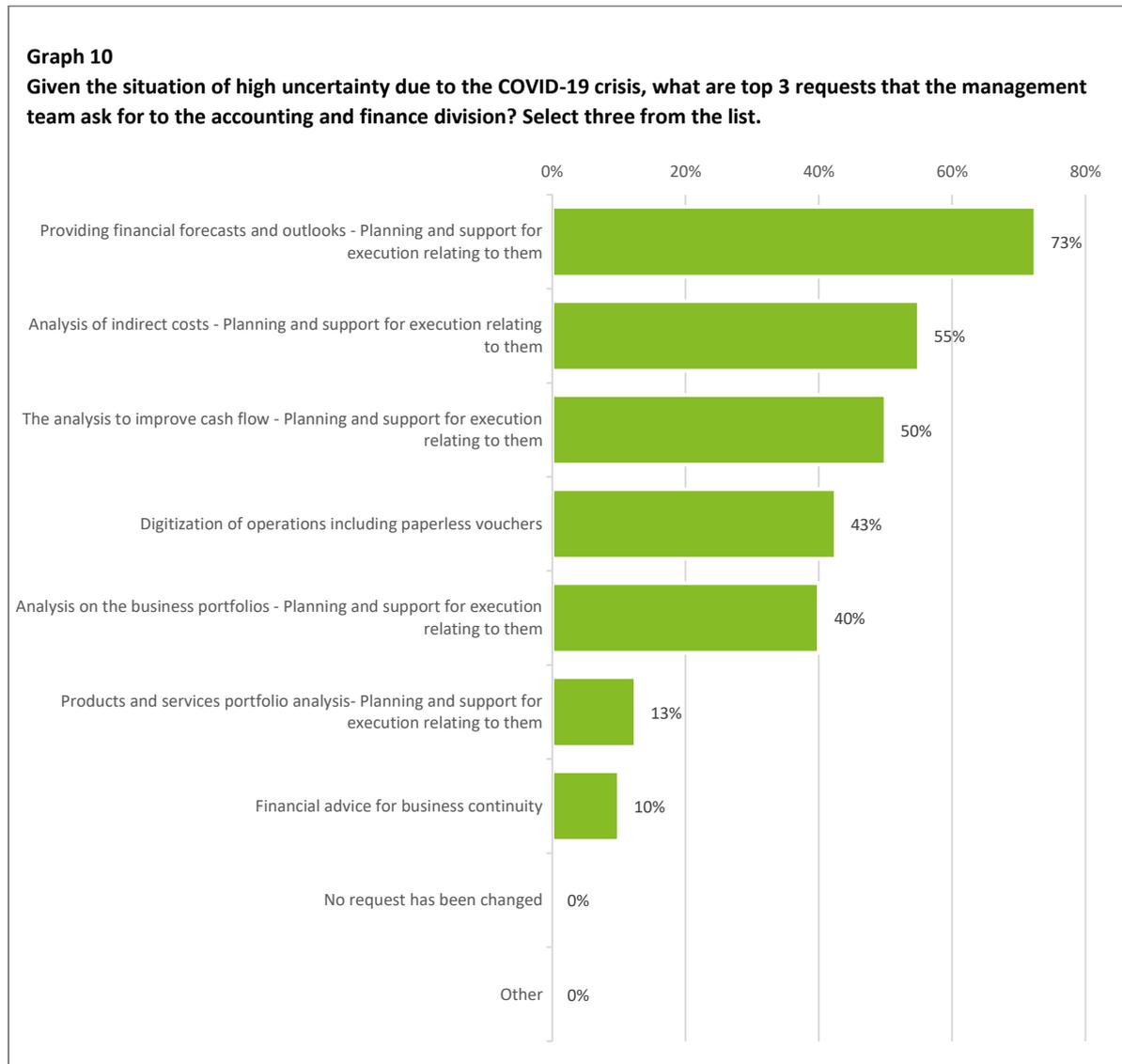
Next, it should be noted that “disclosure of financial outlook” made it near the top of the rankings. This reveals that many companies have expressed concern over the difficulty of disclosing their financial outlooks publicly.

Adding to above, the financial results for FY 20 March were greatly affected by COVID-19. This implies that many companies are worried about their consolidated closing operations. The burning issue for FY 21’s financial results will be whether companies have taken this situation as an opportunity for change and implemented digital and remote financial closing initiatives.



Changes in management team expectations of accounting and finance divisions

Expectations are high regarding the provision of financial forecasts and outlooks, as well as planning and support for initiatives developed based on results from cost and cash flow analyses.



The results showed that management teams have high expectations of their accounting and finance divisions regarding financial forecasts and outlooks, as well as analysis of indirect costs, cash flows, and business portfolios.

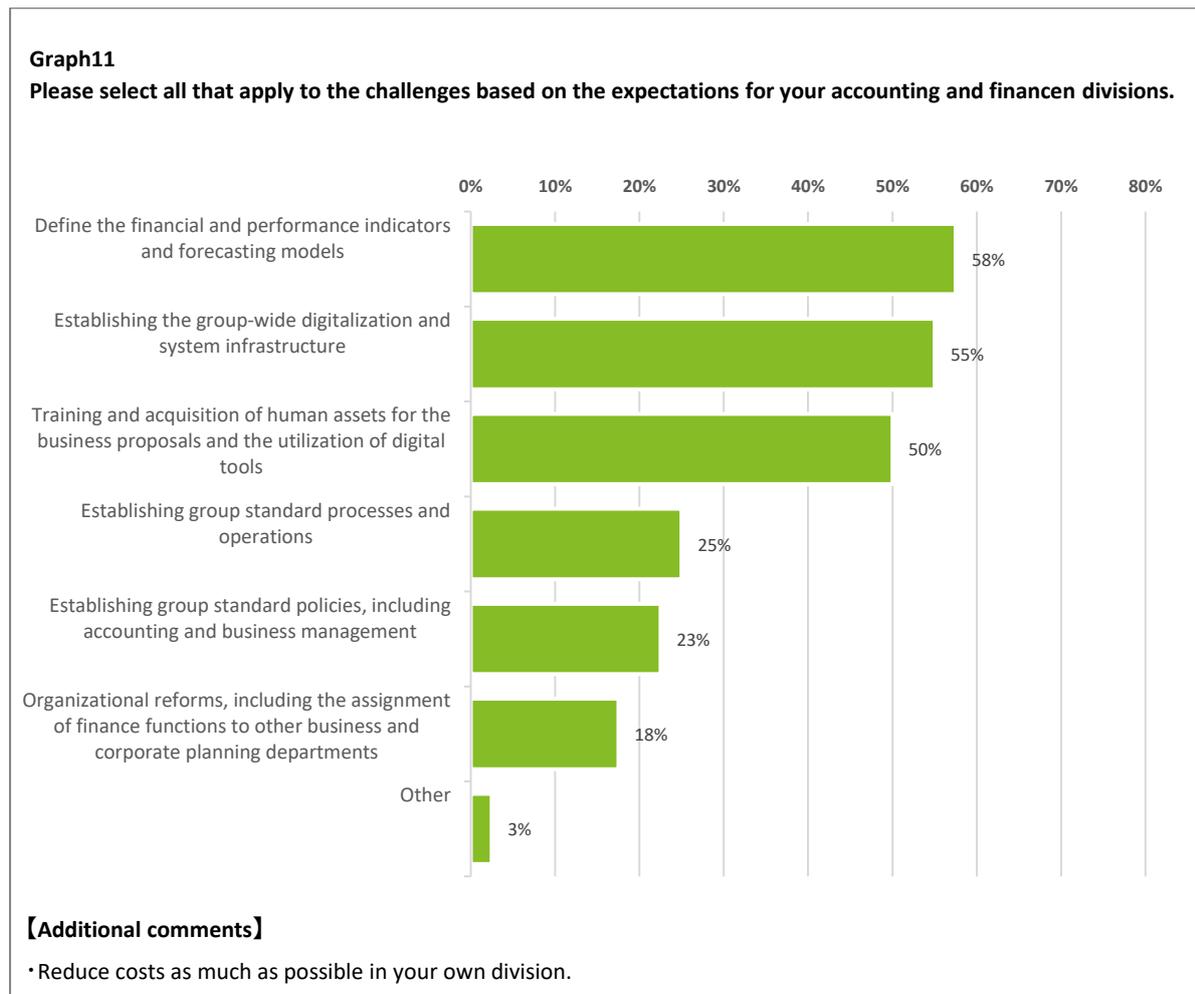
Reduction of indirect costs, redefinition of business strategies, and reclassification of business portfolio ranked high of the management issues investigated in Graph 6. This is consistent with the demand for financial information necessary for such decision-making.

In this high-uncertainty environment caused by the COVID-19 pandemic, the role of the accounting and finance divisions as a business partner to support management and business decision-making will become even more important.



Challenges identified based on expectations of accounting and finance divisions

The top issues were those related to systems, such as the definition of financial and performance indicators and forecasting models, and the establishment of IT systems and digital infrastructures, followed by issues related to the human resources needed to utilize these systems.



The top issues recognized by accounting and finance divisions are the need to define financial and performance indicators as well as forecasting models. This is most likely due to the fact that there is a growing expectation on the part of the management team for the accounting and financial divisions to provide data on financial forecasts and outlooks.

This is followed by the development of company-wide IT infrastructure and digitization. This suggests that there is a need to provide management teams with financial and performance indicators and forecasts in a timely fashion, as well as a need for a mechanism to support focused decision-making, and the digitization of operations, such as paperless vouchers.

In addition to establishing such systems, there is the challenge of developing and/or acquiring human resources who can use these system to support the management team.



Summary

As the COVID-19 pandemic continues to spread, how will companies survive in these uncertain circumstances? How will companies and their CFOs/accounting and finance divisions overcome this situation where all aspects of the business need to be re-evaluated to adapt to the coming new normal?

As companies struggle to reach a conclusion to these challenges, this 2020 Q3 survey focused on management issues and the changing expectations of accounting and finance divisions in these highly uncertain circumstances.

COVID-19 has become a cornerstone in making a clear distinction between strong and weak businesses, and it can be said that an increasing number of companies are redefining their business strategies and reclassifying their business portfolios to rapidly transform their businesses. It is also apparent that more companies are now looking to reduce indirect costs and promote the re-allocation and acquisition of human resources in order to fit their organizations into these new businesses and strategies.

CFOs and accounting and finance divisions are expected to play a leading role by looking ahead and supporting management and business decision-making. There is growing importance of human resources who can support their businesses in reaching the new expectations of their finance and accounting divisions through the use of data infrastructure and analysis models, but the survey results show that many companies feel difficulties in acquiring these resources.

It is expected that the accounting and finance divisions will continue to work on reforms focused on their role in responding to the expectations of management teams.

What is the CFO Program?

The CFO Program is a comprehensive effort by the Deloitte Tohmatsu Group to revitalize the Japanese economy by supporting the CFOs of companies that it rests on and contributing to improving the capabilities of CFO organizations. As a trusted advisor (The Trusted Advisor), we bring together professionals from all walks of life to help CFOs solve challenges. In addition, we aim to improve the competitiveness of Japanese companies by providing the latest information, including global trends, and CFO-networking beyond corporate and industry boundaries.

Deloitte Tohmatsu Group The CFO Program

Marunouchi Nijubashi Building, 3-2-3 Marunouchi Chiyoda-ku, Tokyo, 100-0005

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