



Deloitte CFO Survey

Key Trends

Winter 2016 Results
Research Centre, Moscow

Introduction

Survey goal and objectives

We are pleased to present the findings of the annual Deloitte CIS CFO Survey of the leading companies in Russia.

This is the third time we have conducted the survey in Russia as part of our global research efforts. The opinions provided by the respondents have enabled us to identify major concerns, key drivers, and development priorities for the Russian economy, and to perform a comparative analysis of the existing trends.

The survey was conducted in October 2016, with 60 CFOs responding.

This report was prepared by Deloitte Research Centre, Moscow.

Goal

A comprehensive analysis of trends in the Russian business environment

Objectives

- Determine the outlook for business in Russia for 2016-2017
- Identify expectations for key financial metrics in 2016-2017
- Evaluate the level of uncertainty and key risks of doing business in Russia
- Assess the impact of recent international events on the Russian business environment
- Identify key business strategies and the areas for change
- Identify the drivers and barriers for business in Russia

Methodology Respondents

CFOs of leading companies from key economic sectors.

Methodology

Data was collected through an online questionnaire and personal interviews.

Our comprehensive analysis was based on the following approaches:

01. Identification and examination of general market trends;
02. Comparative analysis of data in meaningful subgroups (analysis of data differing significantly by subgroup and/or from the overall population);
03. Multivariate data analysis (an in-depth analysis of the results to identify hidden differences and incorporate the findings).

Sampling method

The survey was performed on a random sample of respondents from a closed, highly specialised population. The final sample included 60 respondents who were segregated into several industry groups.

Key findings

FINANCIAL PROSPECTS FOR 2017



The general mood is somewhat optimistic:

- 64 percent of the CFOs do not anticipate any positive developments
- 36 percent believe that their company's financial prospects are likely to change for the better

The real estate sector is facing a weakened position:

- The share of pessimistic answers grew by 12 pp.

The best-performing industries are:

- Oil and gas sector (45 pp up)
- Banking sector (8 pp up)
- Manufacturing sector (40 pp up)

In the second half of 2016, the majority of respondents (55 percent) still believed that the best conditions for business can be found abroad. However, Russia has become more appealing to businesses as compared with the beginning of the year (19 pp up).

- In general, the attractiveness of the USA for business in the current economic climate is rated somewhat higher.
- The EU countries are seen as the least attractive region in terms of business outlook.

KEY FINANCIAL METRICS



Overall, the perceptions are quite optimistic. The share of respondents expecting growth in operating profits has increased by 16 pp.

- 61 percent of the CFOs anticipate higher operating profits in 2017, and only 16 percent forecast weaker financial performance
- 78 percent expect an increase in their real income

Negative trends in human resources policies are giving way to more stability and optimism. Companies are striving to retain both the number of staff and the wage/salary levels.

- The share of respondents planning staff cuts has fallen by 10 pp
- The number of companies planning to reduce wages/salaries has fallen by 7 pp
- Almost a quarter of the CFOs (24 percent) intend to increase their staff numbers
- Almost half of the respondents (49 percent) plan to increase wages/salaries

UNCERTAINTY AND RISKY DECISIONS



During the second half of 2016, the aggregate level of certainty about strategic business decisions grew nearly twice, with the overall level of uncertainty falling by 42 pp.

Driven by rising certainty levels, risk appetites have grown significantly over the last six months.

- 47 percent of CFOs think that Q4 2016 is a good time to make risky decisions
- The number of respondents demonstrating a high risk appetite has gone up 33 pp since two years ago

Overall, lower uncertainty and a higher risk appetite suggest that top managers of the leading Russian companies prefer to make carefully considered decisions.

The top-five risk factors that had the greatest negative effect on business development in Russia in 2016:

- Stress in the financial system
- Weaker domestic demand
- Deterioration of cash flow
- Dwindling operating income
- Weak Russian rouble

STRATEGIES AND RISKS



The survey shows that 56 percent of companies have special measures in place to manage currency risks.

CFOs that consider now to be a good time to take risky decisions are more interested in strategies such as:

- On-going cost control
- Cost cutting
- Increasing cash flow

The top-three risk factors that had the highest negative effect on large business in Russia in 2016:

- Weaker foreign demand
- Cost of capital
- Russian deoffshorisation law

The top-three anti-crisis strategies in Russia in 2016:

- Cost cutting
- Reducing leverage
- Reducing financial risks (interest rates, derivatives, etc.)

Overall, 51 percent of companies participating in our survey plan to expand the geography of business relations.

DRIVERS AND BARRIERS



In the second half of 2016, weakening domestic demand became a significant barrier to business development in Russia.

Cost minimisation strategies remain the key driver for business development in Russia. Yet the latest survey shows that strategies aimed at increasing production in Russia have become an important driver.

In 2015 and the second half of 2016, the barriers to the recovery of businesses in Russia still outnumbered the drivers.

Drivers of business development in Russia in 2016:

- Optimisation of production costs
- Increasing production in Russia
- Organic growth

Barriers to business development in Russia in 2016:

- Financial condition
- Weaker domestic demand
- Weak Russian rouble

SOURCES OF FINANCING



The trend from early 2016 continued, with bank borrowing becoming more attractive

- The attractiveness of this source of financing grew by 22 percentage points

Internal financing remains the most attractive source of funding despite a drop of 11 percentage points.

Loans from companies or private individuals have become more attractive to the respondents

- The attractiveness of this source of financing grew by 25 percentage points

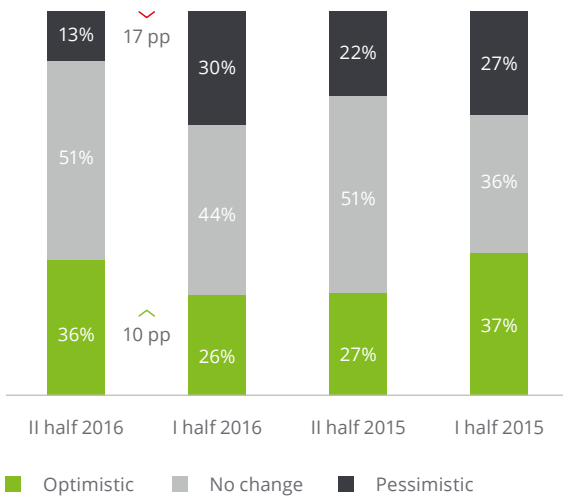
Foreign investments remain essentially just as attractive, with a measured positive outlook

- The attractiveness of this source of financing grew by 7 percentage points

Outlook for business in Russia

Financial prospects

Respondents were asked to assess the financial prospects in comparison with the situation six months ago (spring 2016).



TREND

Over the last six months, the pessimistic sentiments that saw almost one third of CFOs noting negative changes, have been giving way to a cautiously optimistic view. Now, 36 percent of the CFOs note positive changes in the prospects for business.

Significantly, the number of respondents seeing no changes in their financial prospects has risen too. Compared to the recent generally pessimistic views, this suggests that Russian businesses are slowly recovering.

According to the Russian Ministry of Economic Development, the net financial result for large and medium-sized Russian businesses increased by 17.8 percent for the first eight months of 2016. This corresponds to the survey results: the share of negative views has shrunk almost twofold (from 30 to 13 percent).

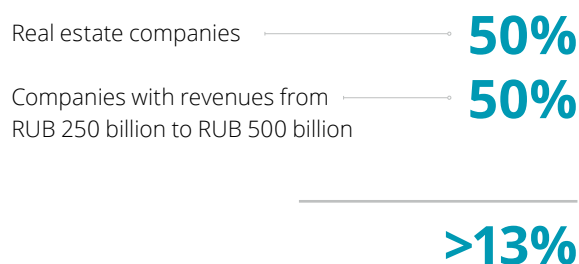




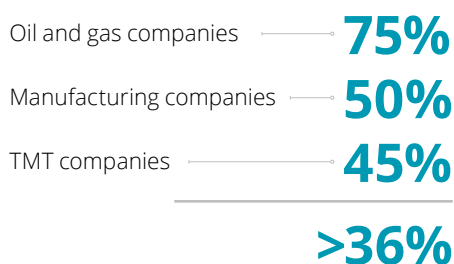
As part of our in-depth analysis, we compared optimistic expectations by subgroup and identified the following significant differences.

TREND

Strongly pessimistic views prevail among:



Strongly optimistic views prevail among:

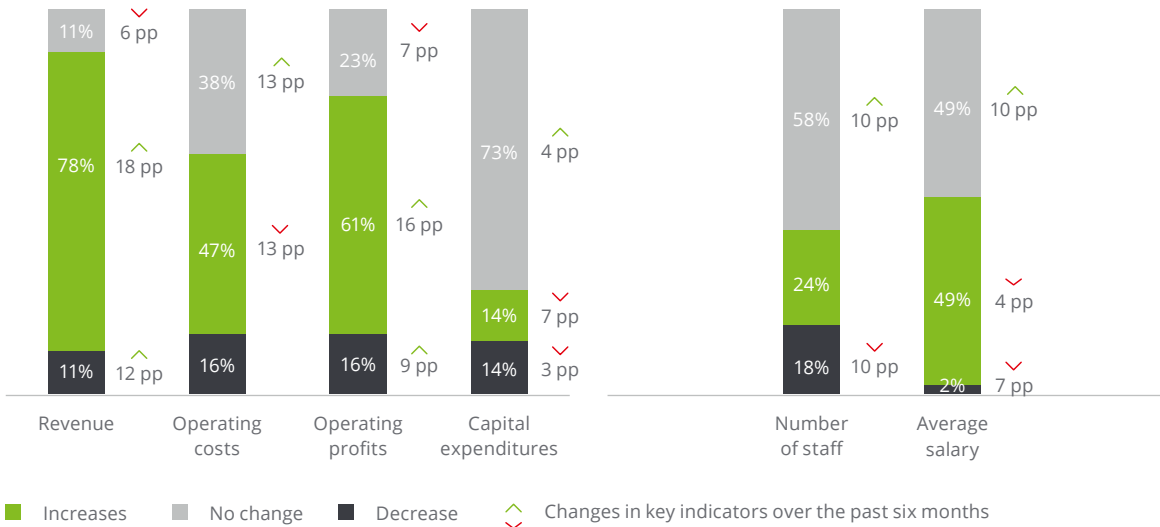


During the second half of 2016, the real estate sector is facing a weakened position, with pessimistic sentiments growing by 12 pp over the last six months. The real estate companies were the only group showing no optimism about their financial prospects. This finding corresponds to Russian Ministry of Economic Development data that suggests that the seasonality-adjusted overall construction volumes consistently fell from January to September 2016 (down 4.4 percent on the same period last year). Oil and gas companies display the opposite trend, with optimistic views growing by **45 pp**. The performance of the manufacturing sector has improved as well. Optimistic sentiments have increased by **40 pp**.

There are some notable changes in the TMT sector. During the first six months of 2016, TMT companies demonstrated high levels of optimism. Today, however, the majority of them (46 percent) do not anticipate any significant changes in their financial prospects. Yet, compared to the previously cited optimistic views, this suggests that the situation is stable, with a positive outlook.

The level of uncertainty in the consumer sector has risen, which is attributable to the deterioration in real income in January to September 2016 (down 5.3 percent on the same period last year, according to the Russian Ministry of Economic Development).

Expected changes in key corporate financial metrics*



TREND

Overall, perceptions are fairly optimistic. The share of respondents expecting growth in operating profits has increased by 16 pp.

The consumer sector tends to anticipate an increase in operating profits **83%**

Pessimistic sentiments are largely expressed by the real estate sector **50%**

No change is expected by the oil and gas sector **50%**

The trends in human resources policies observed during the first six months of 2016, are no longer relevant. Companies are striving to retain both the number of staff and salary levels. The number of companies prepared to cut their staff numbers has dropped by 10 pp, and the number of those planning salary cuts, has decreased by 7 pp.

Increases in the number of staff are mostly planned by foreign companies **43%**

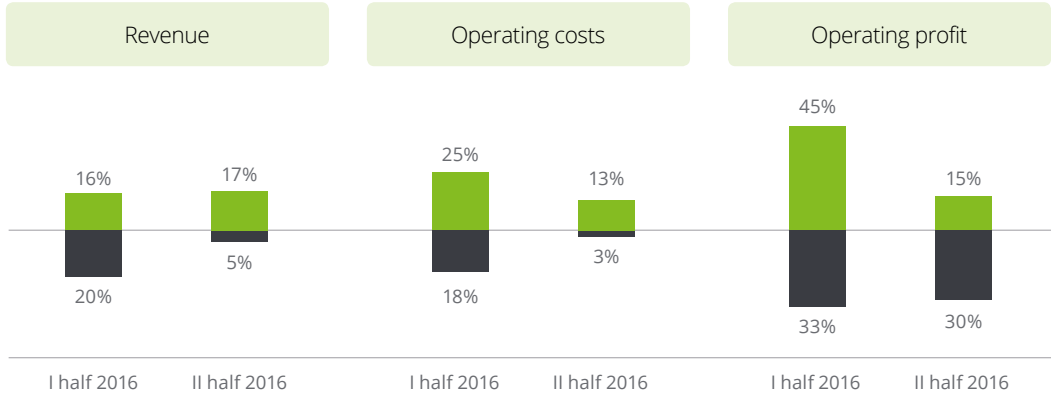
Staff cuts are generally anticipated by the real estate sector **50%**

Salary increases are primarily planned by pharmaceutical companies **63%**

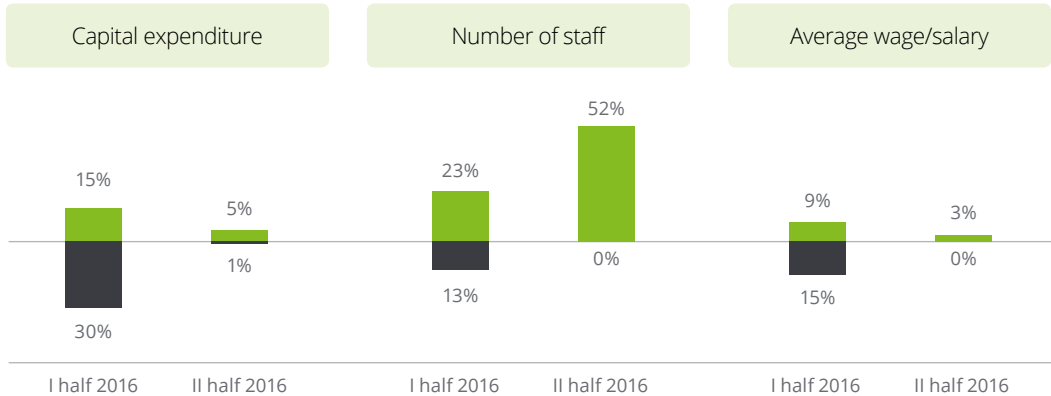
And the banking sector **54%**

* All metrics in rouble equivalent

Matrix of expected changes in key corporate financial metrics*



- The average expected decrease in revenue is 5 percent.
- The average expected increase in revenue is 17 percent.
- The average expected decrease in operating expenses is 3 percent.
- The average expected increase in operating expenses is 13 percent.
- The average expected decrease in operating profits is 30 percent.
- The average expected increase in operating profits is 15 percent.



- The average expected decrease in capex is 1 percent.
- The average expected increase in capex is 5 percent.
- The average expected increase in the number of staff is 52 percent.
- The average expected increase in the average salary is 3 percent.

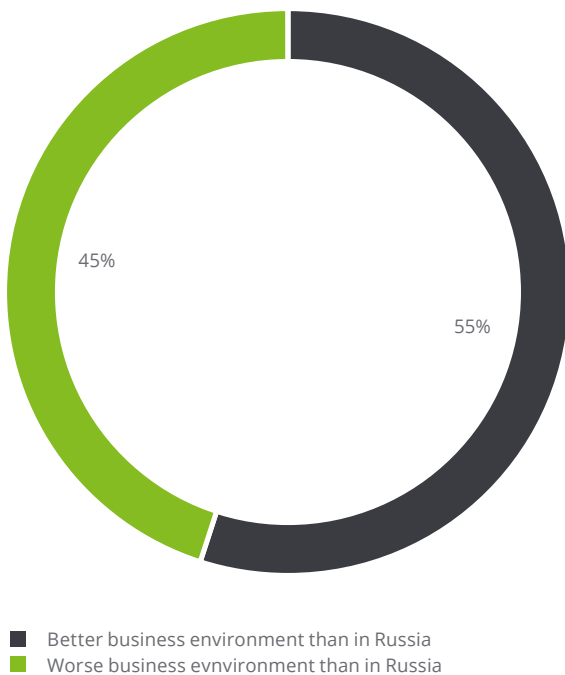
■ Up
■ Down

* All metrics in rouble equivalent



Prospects of doing business abroad

Based on perceptions of the current business climate in other countries



TREND

TMT companies generally find Russia more attractive for business (60 percent).

The banking and oil and gas sectors find foreign markets more appealing (by 6 pp and 15 pp, respectively).

The top-three most attractive countries

- USA
- China
- Kazakhstan

The top-three least attractive territories

- EU
- CIS
- Ukraine

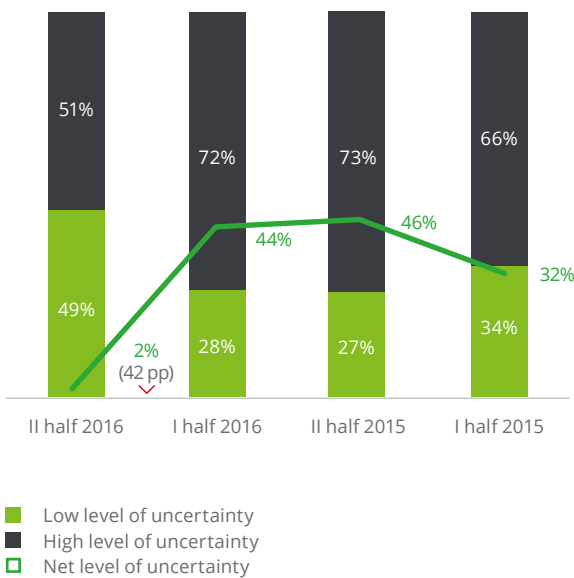
In early 2016, large Russian businesses generally considered Europe to be a good place for doing business, but by the end of 2016 this trend has reversed.

In the second half of 2016, the majority of the respondents (55 percent) believed that the best conditions for business can be found abroad.

However, Russia has become more appealing to businesses as compared to the beginning of the year (19 pp up).

Uncertainty and risks

Uncertainty in strategic decision making



TREND

The rising levels of uncertainty observed over the past two years have dropped dramatically by 42 pp since the first half of 2016.

49% of CFOs rate the level of uncertainty as low.

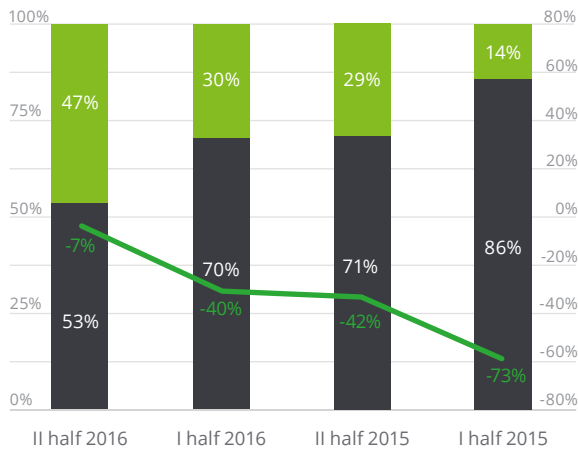
The most significant change is demonstrated by the TMT sector, with **63%** of companies citing low levels of uncertainty in strategic decision making, which is two times less than six months ago.

The highest levels of uncertainty (**75%**) are reported by the oil and gas sector.

The banking sector also rates the level of uncertainty as high (**62%**).



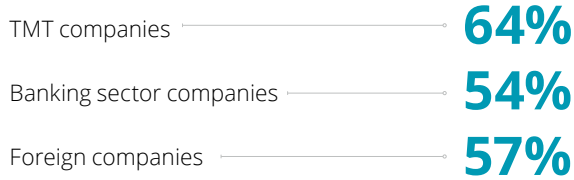
Risk appetite



■ Yes
■ No
— Risk appetite

TREND

The highest risk appetites are demonstrated by:



Over the last two years, the risk appetites of large businesses in Russia have changed drastically. In early 2015, the overwhelming majority of the CFOs were not ready to make risky decisions. In late 2016, the number of those who believe it is a good time to make risky decisions have increased 3.4 times.

The second half of 2016 witnessed a sharp growth in risk appetites (**33 pp up**).

The real estate sector is the only group demonstrating lower risk appetites and sector reports the lowest level of optimism in assessing the current economic situation. In early 2016, 63 percent of the real estate companies surveyed indicated that they were not ready to take risks, but in late 2016, the share of such companies has grown to 100 percent.

Key risk factors in the second half of 2016

TREND

The fourth round of our survey shows that the top-five risk factors dominating earlier in the year have only strengthened their positions. Increasing references to stress in the financial system once again prove that the events of late 2014 are having a long-lasting effect and the Russian economy (and big business in particular) is recovering slowly.

The top-five risk factors that had the greatest negative effect on business development in Russia in 2016 are:

- Stress in the financial system
- Weaker domestic demand
- Deterioration of cash flow
- Dwindling operating income
- Weak Russian rouble

The risks associated with the stress in the financial system and the weak domestic demand are critical to the companies operating in the banking sector.

Deterioration of cash flow has the worst effect on the consumer sector.

Why don't CFOs see any improvement in their companies' situations?

Pessimistic financial expectations are driven by:

- Increasing business regulation in Russia
- Shortage of capital
- Geopolitical risk

Risk factor map

After a detailed analysis of the data, we aggregated the risk factors into a risk map, which allowed us to assess the effect and the nature of the influence each of them has on two performance indicators: the expected annual operating profits for 2016 and the general perception of the current financial prospects.

The risk map also helps to identify hidden risk factors, which the CFOs believe to have a significant negative effect on business development in Russia.

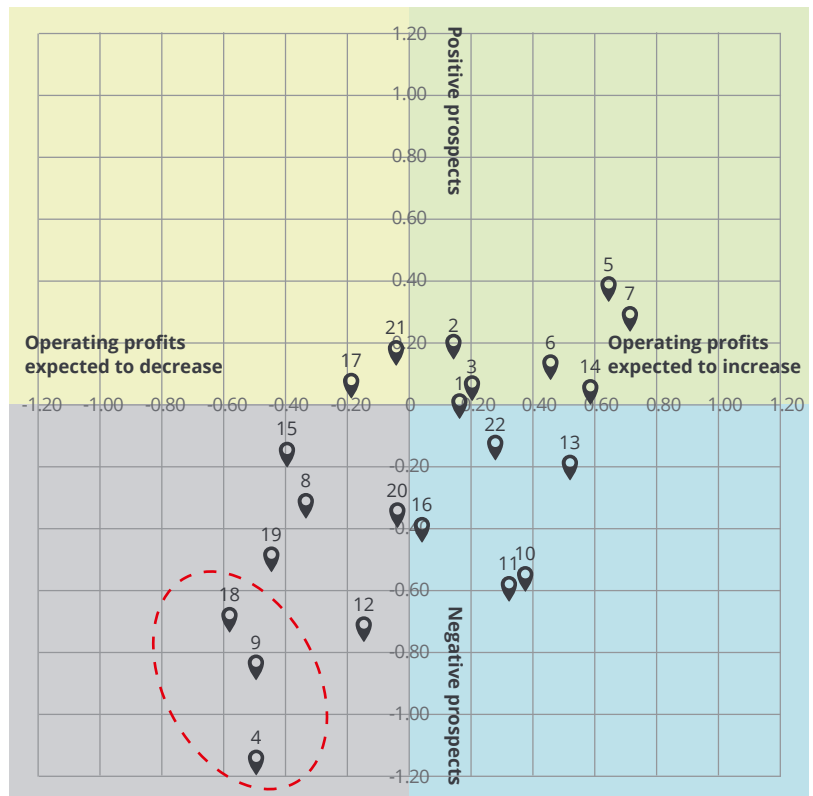
The risk map includes four zones:

Zone 1. Favourable zone: companies expect growth in their operating profits and report improved financial prospects.

Zone 2. Medium risk zone: companies expect falling operating profits, but report improved financial prospects.

Zone 3. Medium risk zone: companies expect growth in their operating profits, but report a deterioration in financial prospects.

Zone 4. Unfavourable zone: companies expect falling operating profits and report deterioration in financial prospects.



Risk appetite

TREND

The risk factors in zone 4 are characterised by a raised negative effect:

- Weaker foreign demand (#4)
- Cost of capital (#9)
- Russian deoffshorisation law (#18)

#	All the considered risk factors	I-2015	II-2015	I-2016	II-2016
1	Stress in the financial system				
2	Weak Russian rouble				
3	Weaker domestic demand	●			
4	Weaker foreign demand				●
5	Rising labour costs				
6	Rising domestic input costs		●		
7	Rising foreign input costs				
8	Deterioration of cash flow	●			
9	Cost of capital				●
10	Shortage of capital				
11	Rising barriers to trade/protectionism	●		●	
12	Increasing business regulation in Russia				
13	Geopolitical risk				
14	EU sanctions against Russia	●			
15	Russia's embargo on foodstuffs		●		
16	Potential reciprocal non-food sanctions by Russia (gas, wood, etc.)		●	●	
17	Potential reciprocal food sanctions by EU				
18	Russian deoffshorisation law				●
19	Dwindling operating income	●		●	
20	Rising barriers to entry into new markets				
21	Decreasing consumer interest in new products				
22	Reduction in informational transparency				



International events and their impact

The prevailing trend over the past years still persists at the end of 2016: sanctions, FX, and the deoffshorisation law remain among the critical international factors affecting large businesses in Russia. In autumn 2016, the list was extended due to the suspension of the free trade agreement between Russia and Ukraine.

TREND

The survey shows that by the end of 2016 the negative effect of sanctions decreased by 20 pp to **47%**.

The negative effect of currency fluctuations has remained broadly unchanged.

The negative effect of increasing EUR and USD rates has risen from **37 to 42%**.

The negative effect of the suspension of the free trade agreement between Russia and Ukraine and the deoffshorisation law were rated to be at the same level (**27%**).

EU sanctions against Russia

- Our survey suggests that 45 percent of the respondents do not feel any negative effects from the EU sanctions.
 - This view is primarily expressed by the TMT and manufacturing sectors (64 and 63 percent respectively).
- The sanctions have a greater negative effect on the oil and gas and banking sectors (100 and 62 percent respectively).
- The negative effect of sanctions is noticeable for both foreign and Russian companies (57 and 50 percent respectively).

Weak Russian rouble

- The consumer sector is more susceptible to the weakening of the Russian rouble (79 percent of the respondents report negative consequences).
- It is worth noting that the increasing EUR and USD rates have had a positive effect on 50 percent of the TMT companies surveyed.

Suspension of the free trade agreement between Russia and Ukraine

The suspension has the worst consequences for the oil and gas and real estate sectors (50 percent each).

Risk management

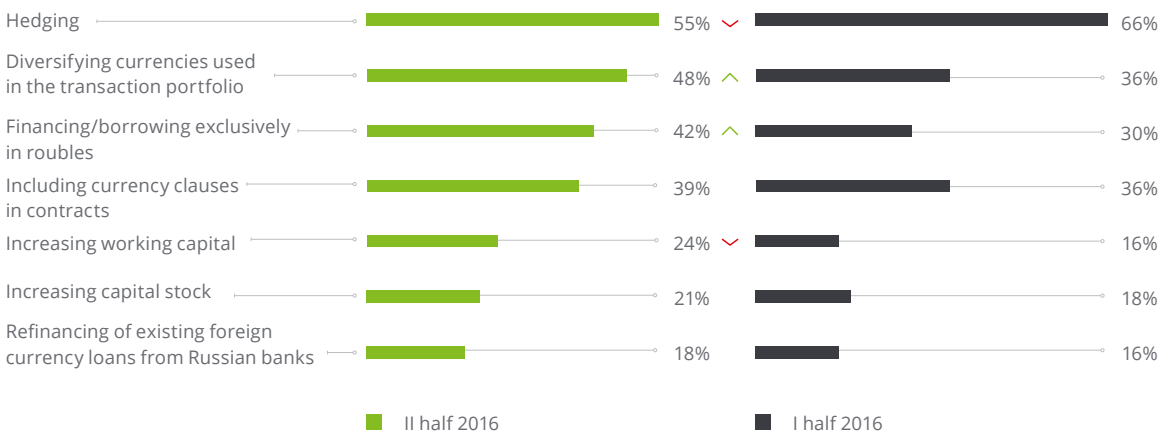
Currency market volatility makes risk management extremely relevant. Just as six months ago, we asked the CFOs how they manage currency risks. We were particularly interested in whether they have special measures in place to address this matter.

TREND

The survey shows that the share of companies employing currency risk management practices has decreased by 14 pp to **56 percent**.

- Risk management is more often used by the consumer sector and the real estate sector (86 and 100 percent respectively).
- While financial hedging is losing its popularity (11 pp down), the practice of diversifying currencies used in the transaction portfolio and financing exclusively in roubles have become more attractive (12 pp up).
- The same trend is observed for the practice of increasing capital stock (15 pp up).

Risk management methods



Business strategies

Strategy attractiveness

TREND

Our research suggests that over the past two years the preferred growth strategies in Russia have remained reasonably stable.

Top-five strategies:

- Restructuring costs (as part of ongoing cost control)
- Ongoing cost control
- Cost cutting
- Increasing cash flow
- Organic growth
- New products/services

Significantly, in the second half of 2016, other growth strategies became relevant, such as

- Investing in human resources
 - This strategy is particularly attractive to companies in the real estate sector
- Reducing currency risks
 - This strategy is particularly attractive to companies in the consumer and oil and gas sectors
- Expansion into new markets
 - This strategy is preferred by companies in the consumer and TMT sectors

Strategies as a result of business positions

Which strategies do CFOs with a higher risk appetite prefer?

Respondents who believe that now is a suitable time for risky decisions tend to be interested in strategies such as:

- Ongoing cost control
- Cost cutting
- Increasing cash flow

How do optimistic CFOs differ from pessimistic CFOs?

CFOs who take a positive view of the financial prospects for their company are strongly inclined towards strategies such as:

- Ongoing cost control
- Organic growth
- Increasing cash flow

Pessimistic CFOs prefer strategies such as:

- Cost cutting
- Organic growth
- Increasing cash flow

Strategy map

A deep analysis of the data allows us to present the growth strategies for 2016 in the form of a strategy map. Using the map, we can determine the most attractive strategies according to companies' financial positions and growth perspectives.

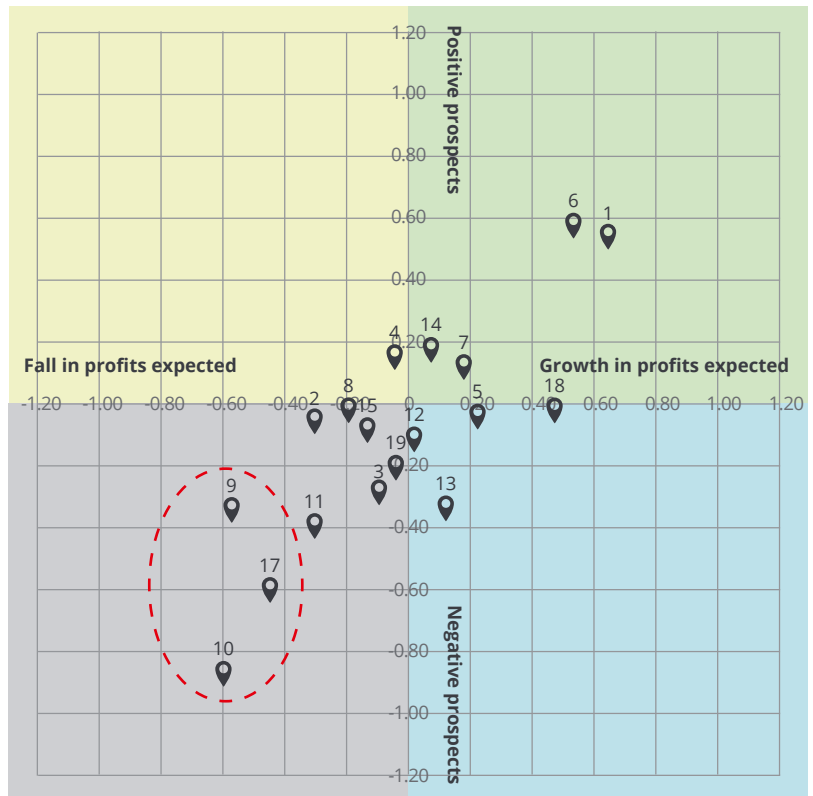
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Zone 4. Unfavourable zone: companies expect falling operating profits and report deterioration in financial prospects.



Anti-crisis measures

TREND

The top-three growth strategies in Zone 4 can be defined as anti-crisis measures:

- Cost cutting (#9)
- Reducing leverage (#10)
- Reducing financial risks (interest rates, derivatives, etc.) (#17)

Whereas strategies in the first half of 2016 were aimed at more active growth, the anti-crisis measures witnessed in the second half of 2016 can be characterised as “defensive”:

- Reducing leverage replaced raising capital from external sources
- Disposing of assets replaced increasing cash flow

#	All the considered strategies:	I 2015	II 2015	I 2016	II 2016
1	Increasing capital expenditures				
2	Acquisitions in Russia		●		
3	Acquisitions abroad				
4	Organic growth				
5	Expanding into new markets				
6	Introducing new products/services	●			
7	Raising dividends or undertaking share buy-backs				
8	Ongoing cost control				
9	Cost cutting	●	●	●	●
10	Reducing leverage				●
11	Disposing of assets	●			
12	Increasing cash flow			●	
13	Reducing currency risks				
14	Increasing R&D spending				
15	Increasing production abroad				
16	Increasing production in Russia		●		
17	Reducing financial risks (interest rates, derivatives, etc.)	●	●		●
18	Investing in human resources				
19	Raising capital from external sources			●	

Prospects for cooperation with foreign companies located abroad as regards business development in Russia

Cooperation with foreign companies is a key issue and its importance has not changed for the respondents since the first half of 2016.



TREND

An absolute majority (**73** percent) report that they cooperate with companies abroad.

Overall, **51** percent of companies participating in our survey plan to expand the geography of business relations. Only **16** percent do not cooperate with foreign companies and do not plan to.

Companies in the consumer and TMT sectors are the most likely to report current cooperation with companies abroad and plans to expand the geography of their business relations – **57** percent and **55** percent respectively.

Manufacturing companies are the most likely to report current cooperation with companies abroad while not planning to expand their pool of partners – **50** percent.

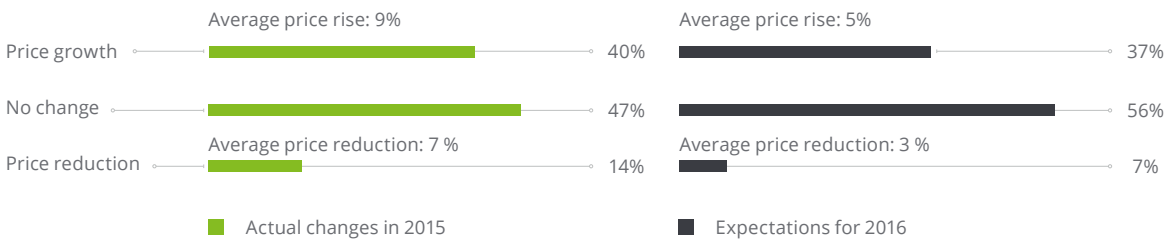
Companies in the banking sector are the most likely to see cooperation with companies abroad as a prospect for the future – **31** percent.

Oil and gas sector companies are the most likely to report having no cooperation with foreign companies and no plans to change this strategy – **50** percent.



According to Rosstat, the consumer price index amounted to 12.9 percent (from the beginning of the year).

However, the consumer price index and the produced price index differ significantly by sector. With this in mind, we asked the survey participants to assess the price movements for their end products and to give their expectations for future pricing policy at their companies.



In 2015, 40 percent of companies increased prices. The average level of price increases amounted to 9 percent.

Of the companies, 47 percent reported no changes in prices.

On the other hand, 14 percent of CFOs reported having reduced prices for end products – on average by 7 percent.

In 2016, the CFOs expectations suggest that 37 percent of the companies intend to raise prices – the average level of expected price growth is 5 percent.

Price reductions are only being considered by 7 percent of the respondents and the average level of expected reductions amounts to 3 percent.



Drivers and barriers

Integration of risk and strategy analysis results

Our analysis of the risk factors and growth strategies allowed us to identify drivers of and barriers to growth for companies on the Russian market in 2016.

BARRIERS



- Weaker domestic demand
- Financial condition
- Weak Russian rouble

DRIVERS



- Optimisation of production costs
- Production in Russia
- Organic growth

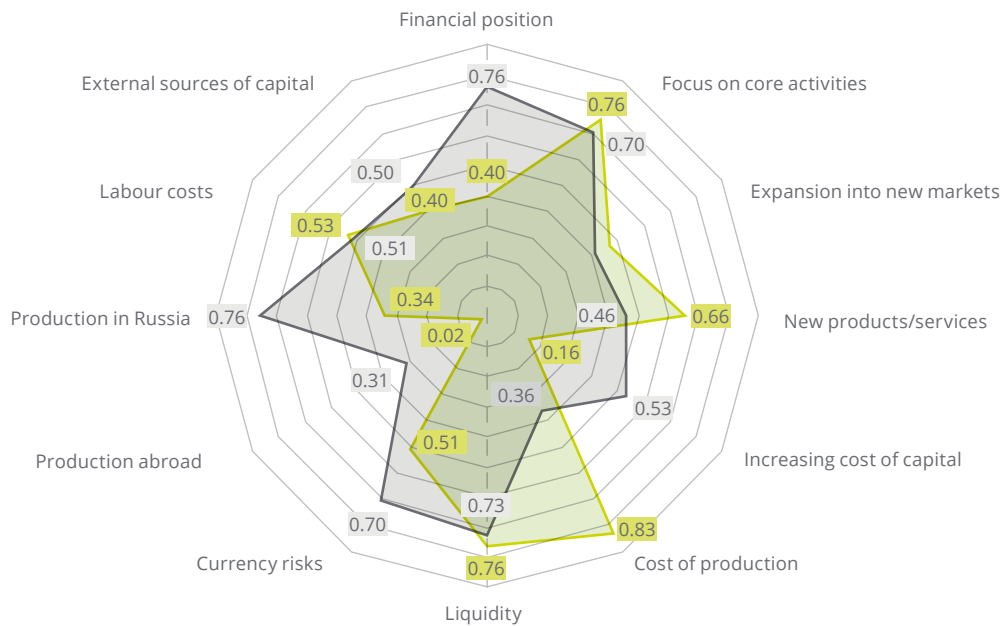
TREND

The barriers to business development in Russia which we identified in 2015 remain in place.

In the second half of 2016, financial condition, production in Russia and liquidity are significant barriers to business development. A comparative analysis reveals that the financial climate in the

country has become an even greater direct barrier to business. This suggests our conclusion that the crisis of late 2014 will have long-term negative effects on big business in Russia remains valid.

The main drivers of growth remain optimising production costs and focusing on core activities.



■ Barriers
[0;1] is value of the effect as a barrier

■ Drivers
[0;1] is value of the effect as a driver

Sources of financing

Attractiveness of sources of financing

Based on our respondent's answers, we identified the most attractive sources of financing (top three). Furthermore, a comparative analysis of the most recent results and the results from the first half of 2016 reveals trends in Russian businesses' decision making as regards sources of financial support.

Top-three sources of financing:

- Internal finance
- Bank borrowing
- Debt raising (borrowing from companies or individuals)

TREND

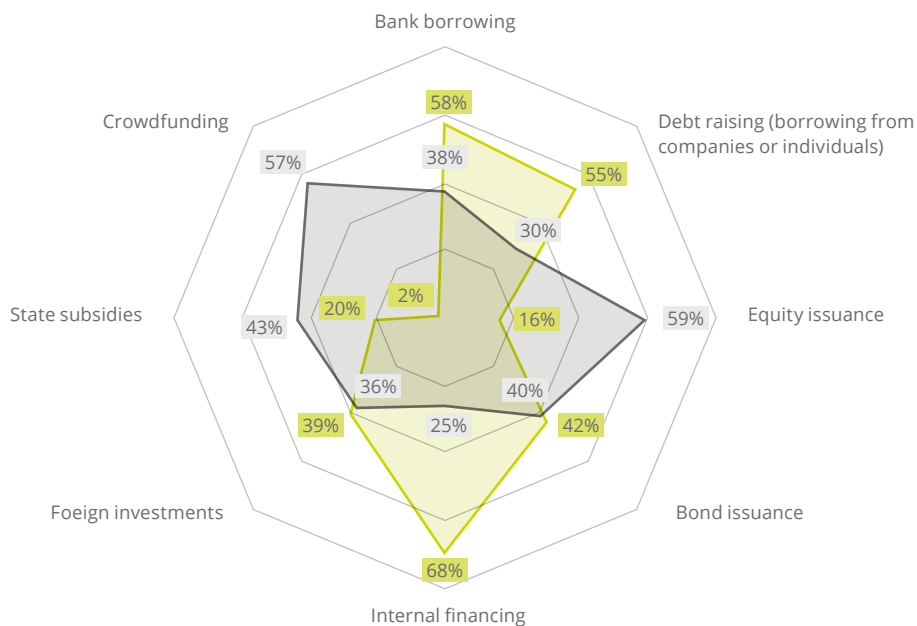
In comparison with the beginning of 2016, CFOs' attitude towards sources of financing has changed a little.

CFOs have warmed towards bank borrowing: the attractiveness of this source of financing grew by 22 percentage points (pp) over the past six months.

There was a measured decrease in the attractiveness of the most popular means of raising capital—internal financing (by 11 pp).

The attractiveness of issuing shares to raise capital fell by 8 pp in the second half of 2016, while issuing bonds became more attractive as a source of financing by 22 pp.

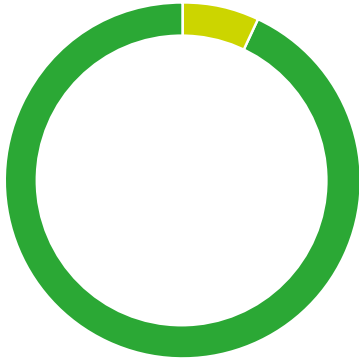
Foreign investments became slightly more attractive by 7 pp.



■ Unattractive
 ■ Attractive

Respondent profile

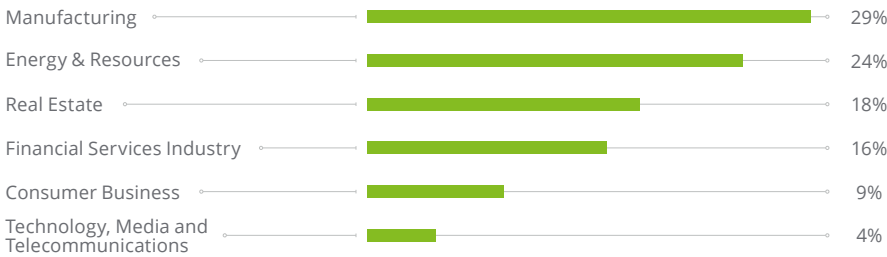
Company type



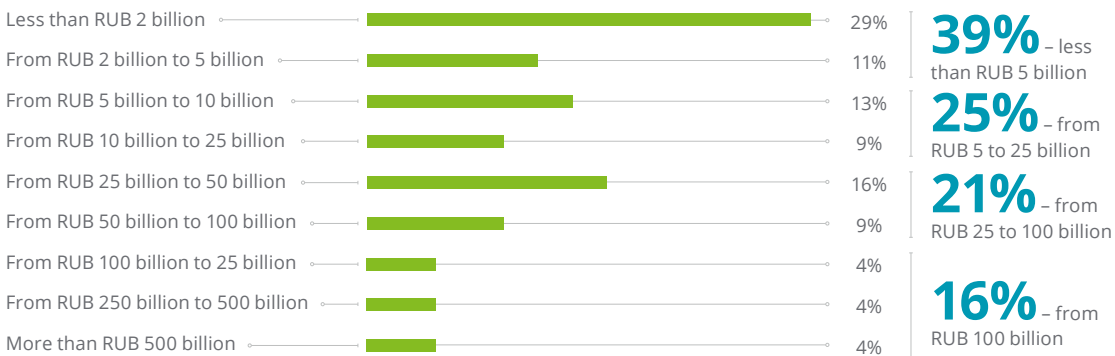
7% – represent foreign companies with localised production in Russia.

The majority – **93%** – represent Russian companies.

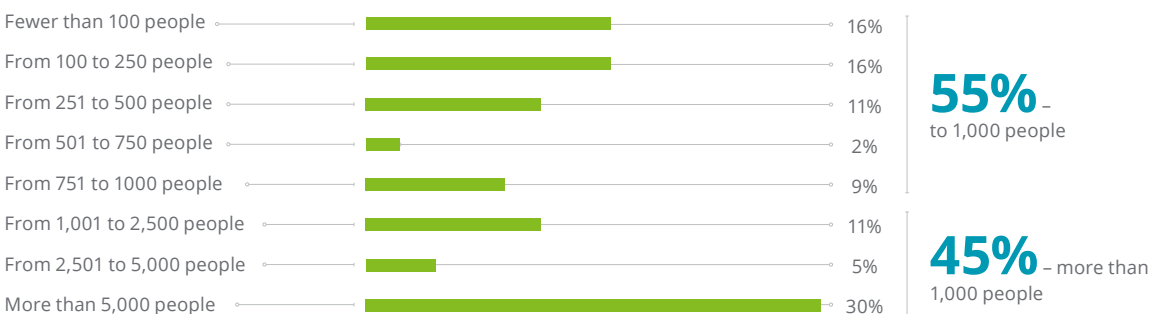
Company sector



Annual income in 2015 (RUB)



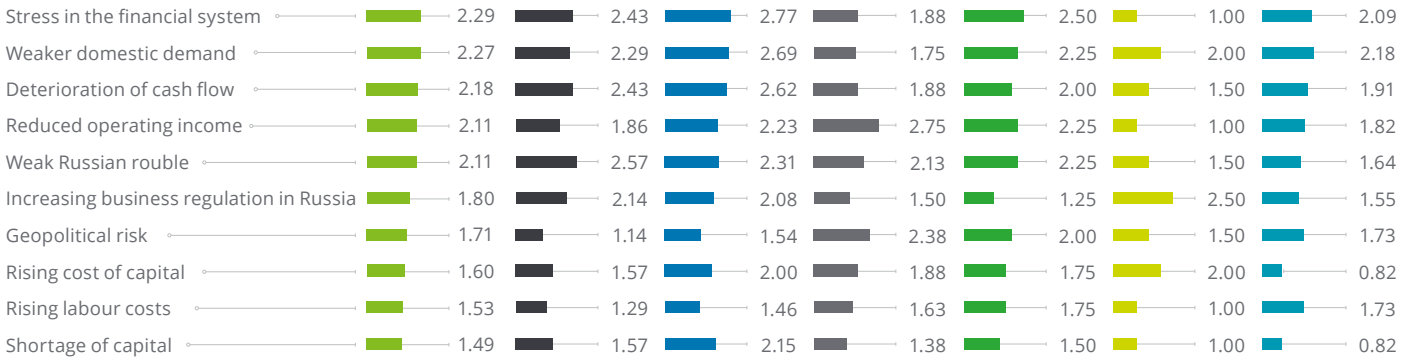
Headcount



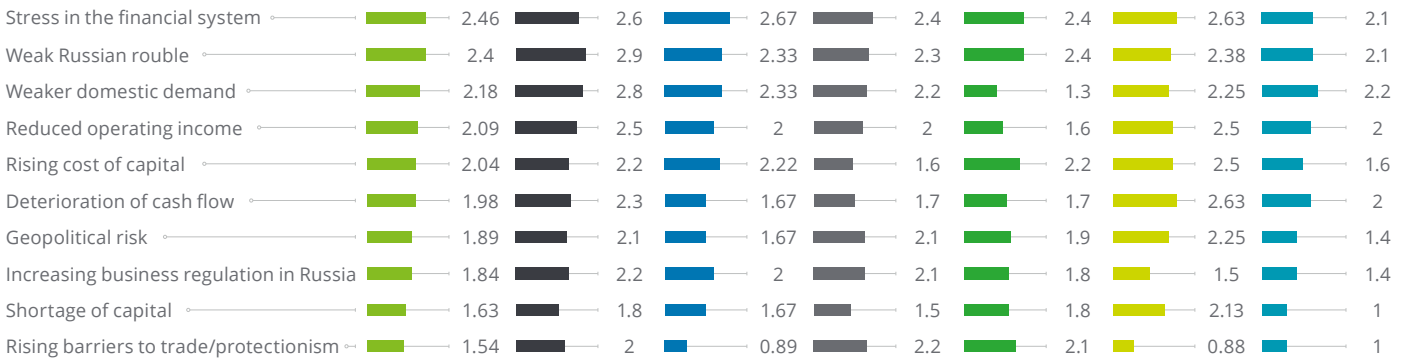
Appendix

Risk rating: Top-10

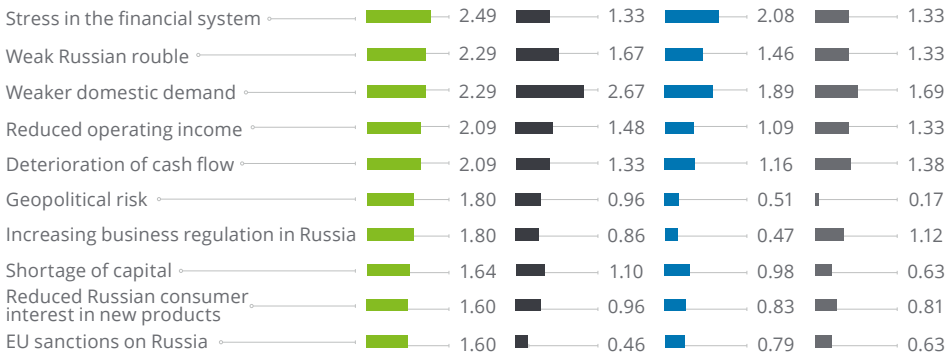
Autumn 2016



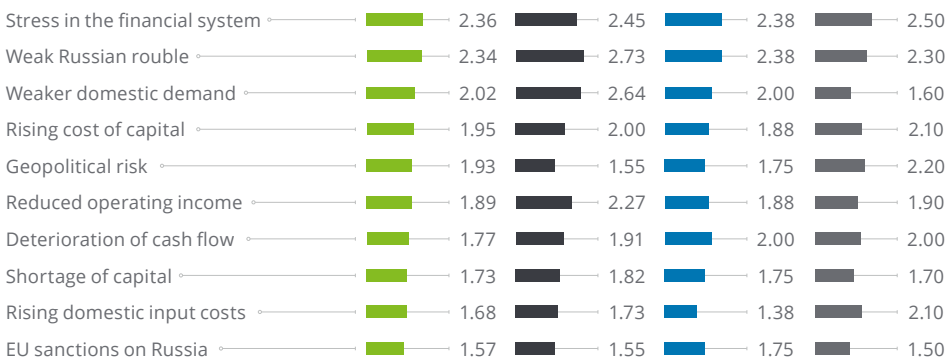
Spring 2016



Autumn 2015

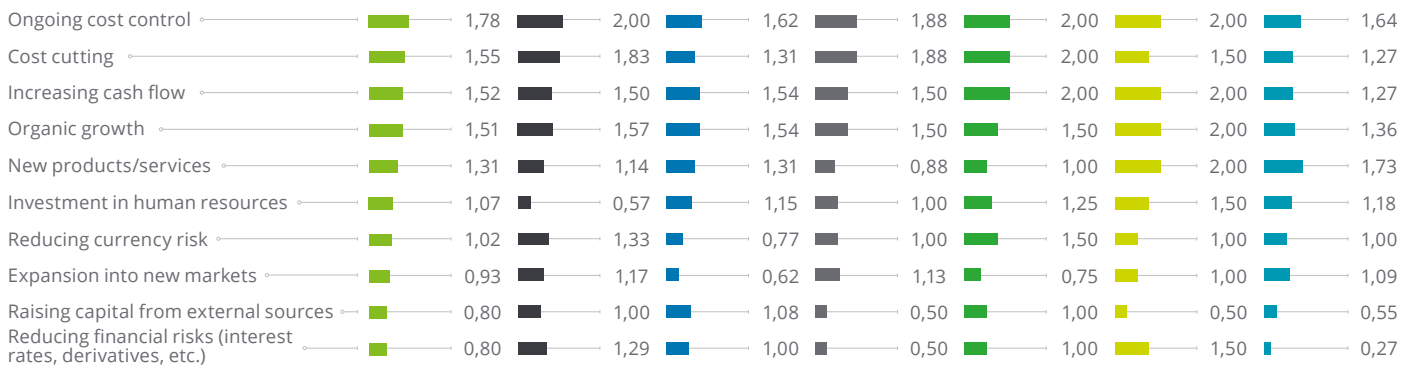


Spring 2015

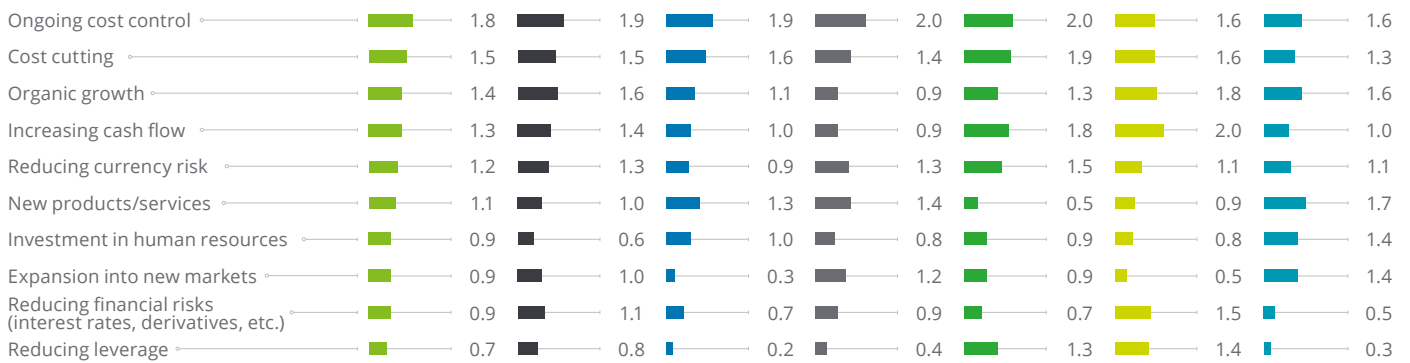


Strategy rating: Top-10

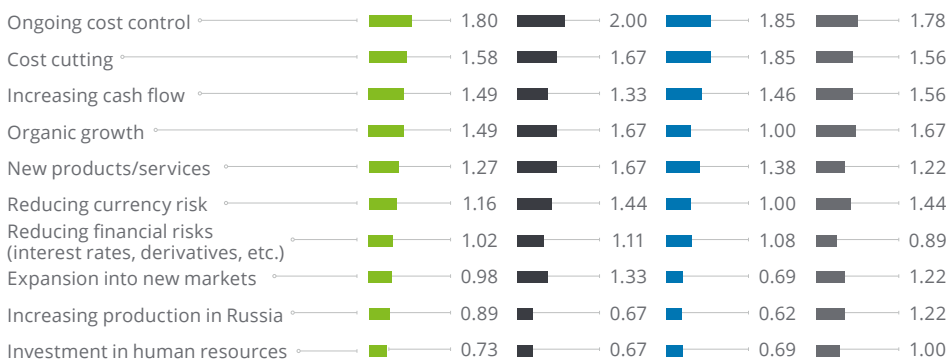
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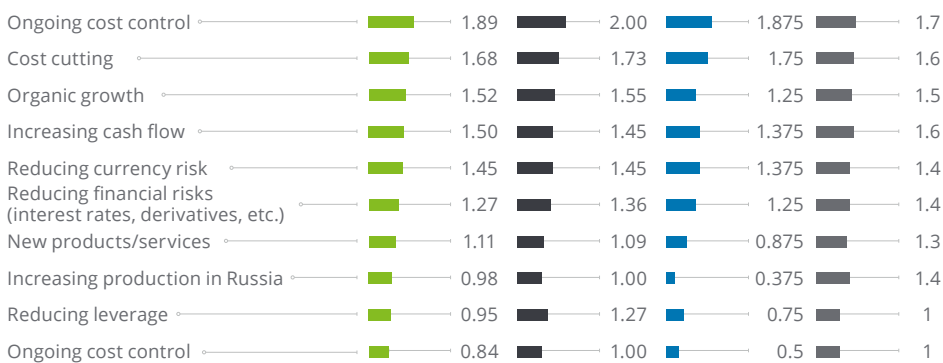
Spring 2016



Autumn 2015



Spring 2015



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If you have any questions regarding the survey, please do not hesitate to contact us.



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