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European CFO Survey

CFOs switch focus to the longer term

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Turkey

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About the data
The findings discussed in this report are representative of the opinions of 1,546 CFOs based in 19 European countries: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, the Netherlands, Norway, Poland, Portugal, Russia, Spain, Sweden, Switzerland, Turkey and the UK. CFOs were all contacted between August and September 2017. Russian responses represent preliminary data.

Some of the charts in the Survey show results as an index value (net balance). This is calculated by subtracting the percentage of respondents giving a negative response from the percentage giving a positive response; responses that are neither positive nor negative are deemed to be neutral. Due to rounding, not all percentages shown in the charts will add up to 100.

Acknowledgements
We would like to thank all participating CFOs for their support in completing the survey. Data management by Ram Sahu.

Further information
For further information and a more detailed analysis please visit www.deloitteresearchemea.com. If you would like to contact us please complete the form on our website or email us at europeanCFO@deloitte.co.uk.

Foreword

Welcome to the sixth edition of the Deloitte European CFO Survey. The Survey presents the insights from CFOs across 19 countries in Europe on market and business sentiment. The political shifts that affected the results in the Q1 2017 survey have now stabilised: this is reflected in a lower perception of uncertainty among CFOs. We see a divide between those based in the euro area and those who are not, with the former markedly more positive about the future. Overall CFOs seem to have turned their focus to the long term and looking at growth prospects. The special questions this edition focus on interest rate expectations, a topic clearly on the mind of central bank policymakers.

The European CFO Survey is an important part of the Deloitte EMEA CFO Programme, an initiative that brings together multidisciplinary teams of senior Deloitte professionals and subject matter specialists across EMEA to help CFOs effectively address the challenges and demands they experience in their role. It is important that we have a clear understanding of what CFOs see as their primary concerns and focus areas.

Overall the Deloitte EMEA CFO Programme helps inform, develop, empower and connect the CFO community across the region. It does this through offerings that include the Deloitte Next Generation CFO Academy and CFO Transition Labs, geared to assist CFOs in executive transitions and transformations. If you would like further information on the programme please contact the programme leader in your country.

We would like to thank all the CFOs who took the time to participate in this edition of the Deloitte European CFO Survey. We hope that these insights bring an interesting dynamic to your discussions.

Alan Flanagan
Partner, EMEA CFO Programme Lead

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CFO Services Lead

Key findings

The message from CFOs in the Q3 2017 Deloitte European CFO Survey is a positive one, with growing optimism, less uncertainty and an increase in employment and investment intentions among most of our respondents.

Improvements in economic conditions are driving this positive mood. Growth outcomes are stronger than expected and forecasts for 2017 and 2018 were revised upwards over the summer, while the OECD countries' consumer confidence is at its highest level for the past ten years.

CFOs are shifting their focus to the longer term, and this is the main message from this quarter. While most indicators are improving, the change is gradual. Perceptions about what is happening in the market are normalising, allowing CFOs to turn their attention to what should come next for their business. This shift in focus is apparent in several ways:

- the outlook for revenue growth is positive
- the biggest positive shift is in CFOs' perception of uncertainty, which is at its lowest level since the beginning of the series in Q1 2015
- hiring expectations are also up, so much so that some CFOs are worried that they will not be able to find the skilled labour they are looking for, or that an increase in demand for skilled workers will price them out of the market
- capital expenditure intentions follow this positive trend: overall CFOs are more willing to spend.

While there is a divergence in sentiment between CFOs in the euro area countries and the non-euro area, these differences are driven primarily by local market conditions.

Interesting differences are also apparent according to company size and industrial sector. Small and medium-size enterprises (SMEs) are under greater competitive pressure, and are turning their attention to recruiting the best talent and raising finance for capital expenditure. As domestic demand picks up, the perception of uncertainty by CFOs in SMEs is lower than for CFOs in larger enterprises. From an industry perspective, CFOs in manufacturing companies stand out as one of the most willing to take on risk, probably driven by their positive expectations for revenues and margins. Those in technology, media and telecommunications (TMT) are also less risk averse, although they are not so optimistic about revenues.

With the economic outlook improving and levels of uncertainty receding, CFOs are able to shift their focus to longer term issues, planning for more expansionary strategies and capital investment. Given the current economic outlook, there seems no better time to face up to the continuing challenges posed by trends in globalisation, digitisation and an aging population.

CFO optimism continues to improve

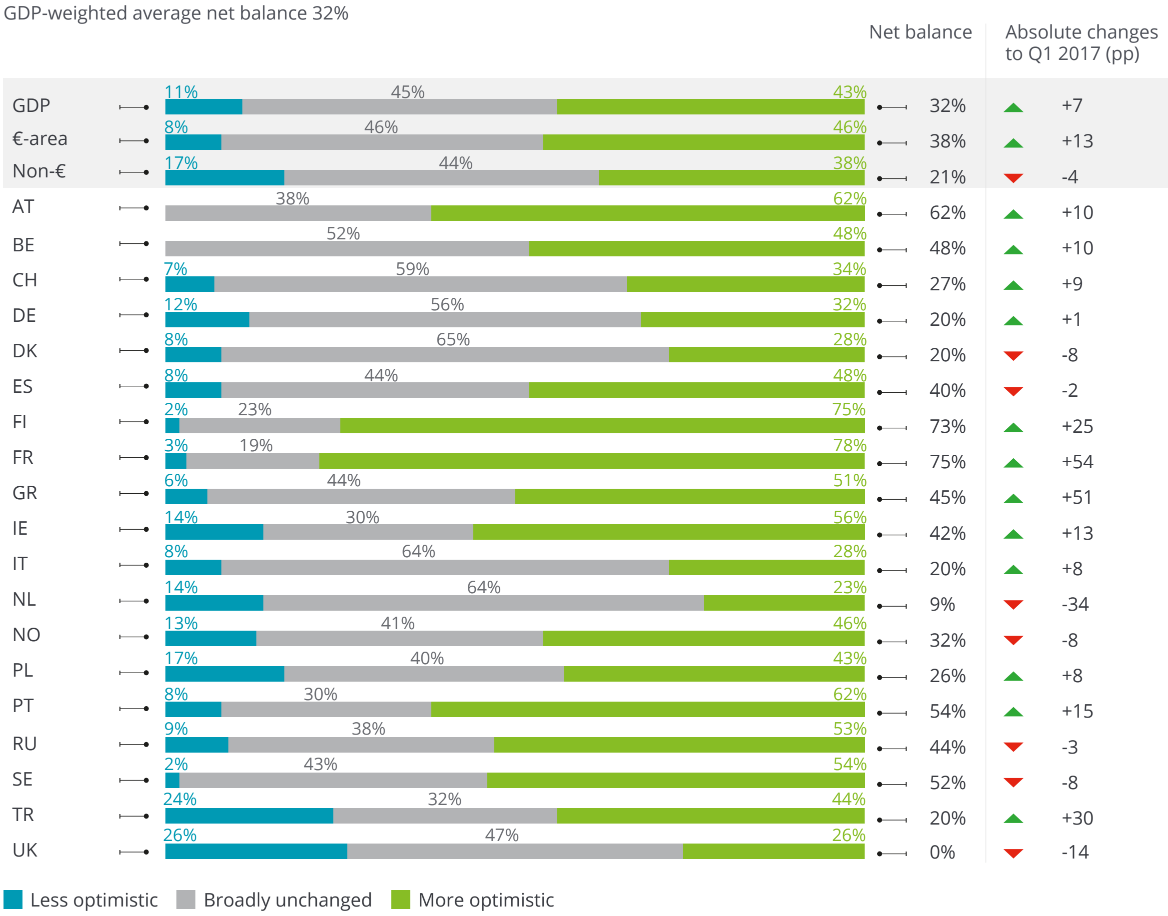
As was the case in the first quarter of 2017 there has been an increase in optimism among CFOs compared to three/six months previously. In Q3 2017 there is a net balance of +32% of CFOs who are more optimistic than pessimistic, the highest amount reached since the beginning of the series. It is also the first time since Q1 2015 that, in all countries, CFOs who are optimistic about financial prospects outnumber those who are pessimistic.

Current economic conditions are driving this positive mood. Growth outcomes have exceeded expectations, and throughout Europe consumer confidence, as measured by the OECD's Consumer Confidence Index, is at a ten-year high. Expectations about growth across the euro area are 0.3 percentage points higher than in April. In addition, unemployment rates have fallen, this summer reaching the lowest level since 2009.

Chart 1. Financial prospects (%)

Compared to three months ago, how do you feel about the financial prospects for your company?*

GDP-weighted average net balance 32%



*Note: In Denmark, Finland, Norway, Italy, Poland, Spain and Sweden the questions specified a six-month period.

CFOs in the euro area are more optimistic

These slightly brighter prospects for the euro area are evident in the views of CFOs, with a net balance of +38% feeling more optimistic, an increase of +13 percentage points (pp) since Q1 2017. The greatest optimism is among CFOs in France (+54pp) and Greece (+51pp). In France this reflects improvements in the economic outlook, with growth forecasts for 2017 upgraded from 1.3% to 1.6% and signs of strengthening across the labour market. Uncertainty surrounding the political landscape is lower: CFO sentiment has been affected positively by newly-elected President Macron's early initiatives to change the labour market laws and simplify the tax code.

In Greece, the improving CFO sentiment is a reflection of how things have started to change. For the first time in three years, the Greek government was able in July to raise money from the bond market. In addition, market expectations around the risk of 'Grexit' have fallen to an all-time low. Although the unemployment rate is still high and private consumption growth was slow in Q2, the European Union's closure of the excessive deficit procedure for Greece was a clear sign to CFOs that the country and its economy are moving forward.

Outside the euro area, sentiment among CFOs is mixed

In contrast to the overall optimistic sentiment within the euro area, the views among CFOs in other countries about financial prospects deteriorated, on average, with the net balance between CFOs who are optimistic to those who are pessimistic falling by 4pp, to +21%. This result was caused largely by a decline in optimism among CFOs in the UK (-14pp), compounded by the GDP weighting assigned to all survey results. Second quarter growth in UK GDP came in at 0.3%, making the UK the slowest-growing economy among the Group of Seven major industrialised nations. With the Brexit-induced fall in the British pound, the UK has recorded one of the highest inflation rates in the industrial world, squeezing real earnings and consumer spending power.

CFO sentiment also declined slightly in Russia (-3pp). Although the country has emerged from recession, the outlook for growth has worsened over the summer. Growth in consumer spending has been weak and is expected to weaken further later in the year, holding back the pace of recovery in the economy. Even so, the most recent consumer confidence index improved for a sixth quarter in a row, indicating that Russian households are becoming more optimistic about their finances and their ability to make major purchases. Thus, despite the small deterioration this quarter, CFO sentiment is still relatively high and is 20pp higher than one year previously.

In contrast to the decline in positive sentiment in the UK and Russia, optimism among CFOs in Switzerland improved for the third time in a row. With a net balance of +27%, optimism about financial prospects among CFOs in Switzerland is at its highest point since Q1 2015. A weaker Swiss franc and sustained demand from European trading partners are clearly influencing this positive sentiment. Indeed, despite a weaker economic performance in the first part of this year, the Swiss government recently raised its growth estimates for 2018 from 1.9% to 2.0%.

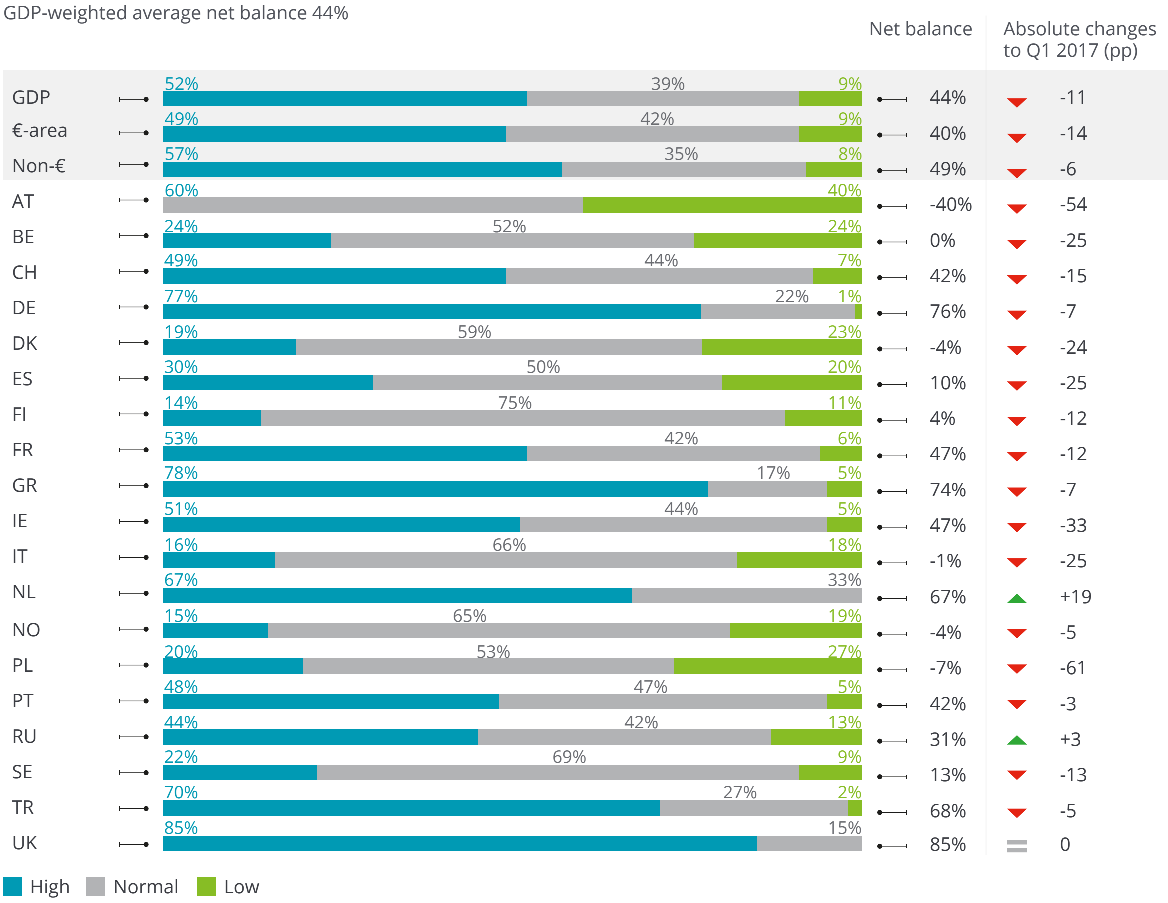
Changing views about uncertainty

Attitudes to environmental uncertainty are a major influence on strategic planning and decision-making, and it is therefore important to understand how CFOs view the level of financial and economic uncertainty their companies are currently facing. In line with the general positive global economic outlook and improved optimism about financial prospects, the perception of uncertainty among CFOs has also improved. The overall net balance is still firmly in positive territory (+44%), meaning that the percentage of CFOs who see 'above-normal' levels of external uncertainty clearly outnumbers the percentage reporting 'below normal' levels. However this net balance fell for the fourth survey in a row (-11pp compared to Q1 2017), to its lowest level since the beginning of the series in Q1 2015. In five out the 19 countries in the survey (Austria, Denmark, Italy, Norway and Poland) the net balance turned negative, signalling a marked reduction in perceived uncertainty.

Chart 2. Uncertainty (%)

How would you rate the overall level of external financial and economic uncertainty facing your business?

GDP-weighted average net balance 44%



Perceptions of uncertainty fell substantially in some countries

Among CFOs in Poland and Italy, there were steep falls in the net balance (by -61 pp and -25pp respectively) between those indicating high levels of uncertainty and those with low perceptions of uncertainty. In Poland, the better-than-expected growth in the first half of the year, and the stabilisation of the state budget (thanks to improved tax collection and buoyant domestic demand) have contributed to the improvement in sentiment among CFOs. Looking at the top external risks identified by CFOs in Poland, 'changes in economic and tax law', which ranked first in Q1 2017, now ranks fourth, while 'additional regulation' dropped out of the top five perceived risks altogether.

In Italy, concerns about the stability of the banking system have receded recently. In July the stock of bad debts in the balance sheets of banks fell to its lowest level since 2014. Political uncertainty also appears to be receding: whatever the results of the elections next year, an abrupt change in government policies now appears less likely, although CFOs do still rank political uncertainty among the top three external risks for their businesses over the next 12 months.

Interestingly, the decline in the overall net balance is driven by a large number of CFOs changing their perception of uncertainty from 'high' to 'normal': the percentage of CFOs indicating a 'low' level of uncertainty remained the same as in Q1 2017.

Geopolitical risks keep the overall level of uncertainly high

Despite the general improvement, perceived levels of uncertainty among CFOs remain high, particularly in Germany and Greece where the net balance is around 75%. This is confirmed by what CFOs perceive as risks, with geopolitical issues still on their minds (see later section on key risks). In Germany, recent elections that weakened the position of Chancellor Merkel may be contributing to this heightened perception of uncertainty.

In this survey, CFOs in the UK are those with the highest perceptions of uncertainty although the net balance is similar to Q1 2017. This sentiment is probably a reflection of the questions that remain unanswered around the Brexit negotiations.

CFOs of larger businesses see a more uncertain environment

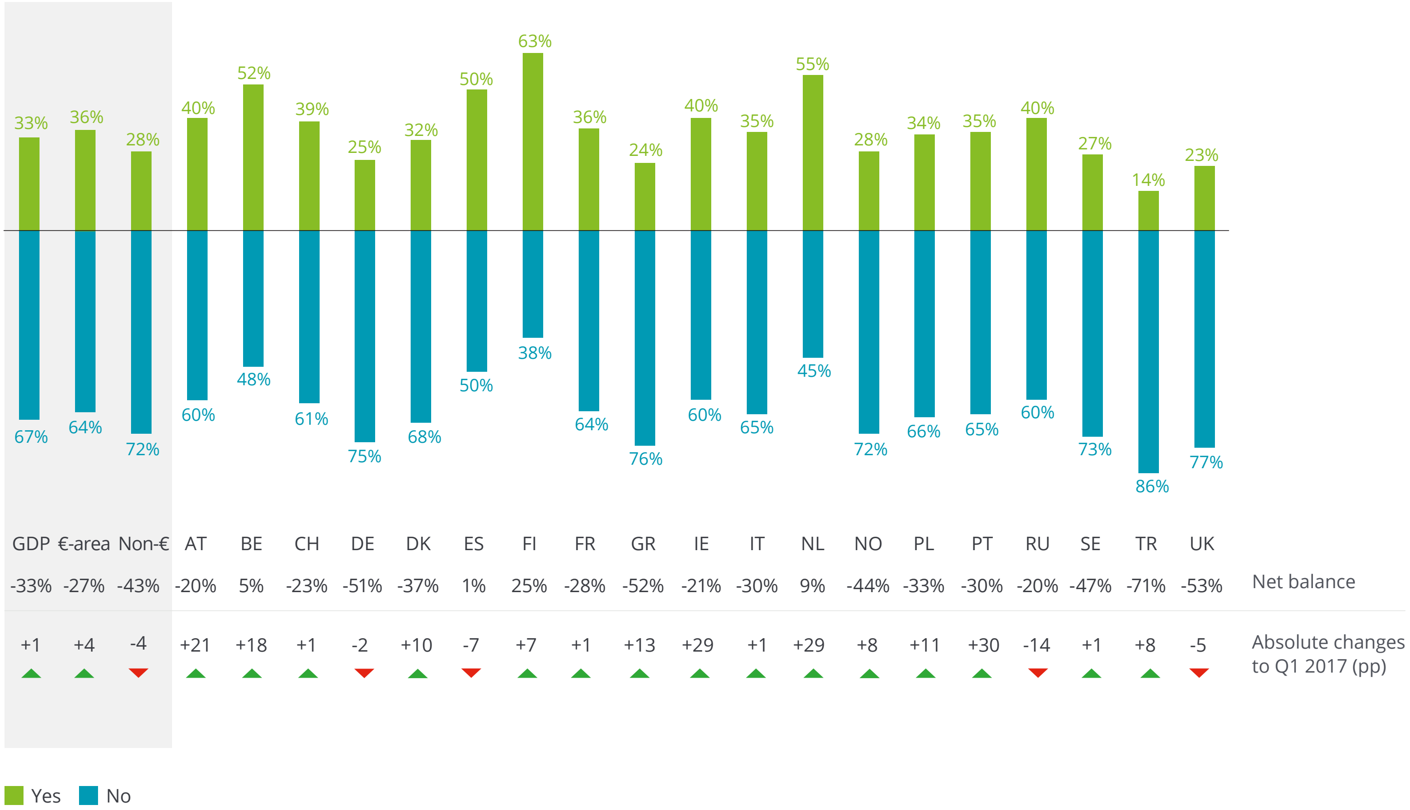
It is also interesting to note that perceptions of uncertainty are higher among CFOs in large businesses (net balance +44%) than among the CFOs in small and medium-size enterprises (net balances of +26% and +30% respectively). It seems that prominent concerns among big-company CFOs relate to issues that might lead to disruption in international trade (such as a rise in protectionism or a collapse in the EU common market).

Risk appetite remains weak but is growing

The overall willingness of CFOs to take on additional risk is substantially unchanged since the beginning of the year. Two-thirds of CFOs indicate that this is not a good time to take on additional risk – the same as in Q1 2017.

Chart 3. Risk appetite (%)
Is this a good time to be taking greater risk onto your balance sheet?

GDP-weighted average net balance -33%



CFOs in the euro area are willing to take on more risk

The overall net balance masks two different trends, among countries inside and outside the euro area. Whereas risk appetite among CFOs, as measured by the net balance, increased by 4pp in the euro countries compared to Q1 2017, outside the euro area it fell by the same amount – driven particularly by a decline in risk appetite among CFOs in Russia and the UK. As in Q1 2017, CFOs in Turkey are the least willing to take on additional risk, although there has been an improvement of +8pp in the overall net balance.

It seems that CFOs remain cautious, adopting a 'wait-and-see' approach, in spite of the reduced level of uncertainty (Chart 2) and the general upbeat mood about financial prospects (Chart 1). It will take time and further signs of reduced uncertainty before the improving sentiment feeds into a more positive attitude towards risk.

Attitudes to risk vary across industries

CFOs in TMT are the most willing to take additional risk on to their balance sheets (net balance -17%), followed by CFOs in the manufacturing sector (net balance -21%). In comparison, less than one-quarter of CFOs in the energy, utilities and mining sector feel that this is the right time to take on greater risk (net balance -52%).

Positive expectations for revenues and margins

CFOs on the whole remain optimistic about revenue prospects for their companies. As in Q1 2017, there is a net balance of 59% of CFOs who expect their revenues to increase over the next 12 months compared to those who expect falling revenues. On average, more than two-thirds of CFOs expect their companies' revenues to grow, compared to just 11% who expect a decline. Although these positive expectations may be driven by the intrinsic role of CFOs to press for higher revenues, the survey results are also consistent with the improving global economic outlook.

There is also a positive outlook for operating margins, with the exception of CFOs in the UK, where 61% expect operating margins to fall over the next 12 months and only 12% expect an increase.

Confidence about revenues greater than for operating margins

Although net balances for both are positive, it is interesting to note that expectations for revenue growth are generally greater than for improving profit margins. In fact, the net balance of CFOs who expect revenues to increase is more than twice as high as for those expecting margins to increase. Furthermore, compared with one year ago (Q3 2016) expectations of revenue growth have increased more (+10pp) than for expectations about higher margins (+5pp). This suggests that, due to competitive conditions in many markets, there will be pressure on margins in spite of increasing revenues, and CFOs may seek to improve operating efficiencies in order to reduce costs. Chart 4.1 combines' revenue and margin expectations and shows the deviation from the (GDP-weighted) net balance. It is possible to see from this the countries in which CFOs may be under most pressure from increasing costs relative to growth in revenue.

The pressure on margins varies between countries

In Sweden and Finland expectations with respect to both margins and revenues are above the overall average and also above their long-term trend. CFOs in these two countries are also the most optimistic about financial prospects (see Chart 1) and expansionary strategies are at the top of their strategic priorities (see Chart 6, Strategic priorities). In Sweden CFOs identify fierce price competition as the second highest risk facing their business.

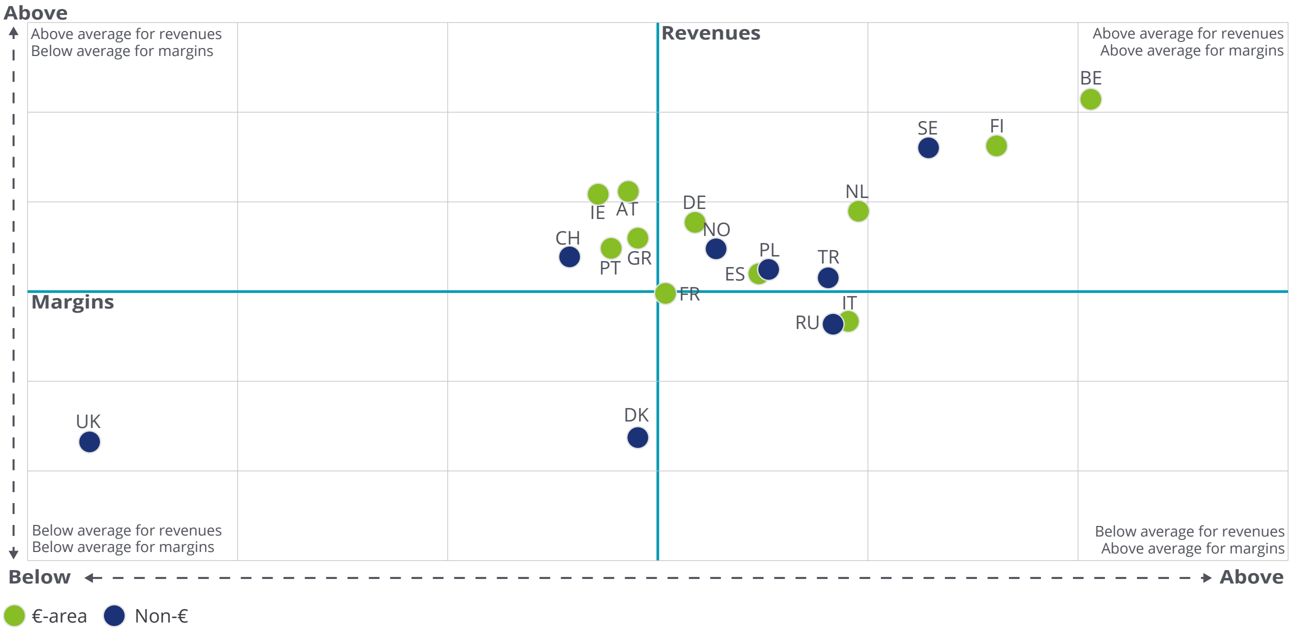
In Ireland, Portugal and Switzerland, revenue expectations are above average, but expectations about profit margins are below. In all three countries, CFOs identify a shortage of skilled labour among the top five risks their company will face over the next 12 months. CFOs in Switzerland explicitly identify pressure on 'prices and margins' among the top five risks for their company. The strong Swiss franc has dented operating margins and currency risks are a strategic concern (see Chart 5). The depreciation in the franc over the summer has come as a relief and might also explain the substantial increase (+10pp) in expectations for profit margins among CFOs in Switzerland since Q1 2017.

In Italy and Russia, on the other hand, expectations are high when it comes to margins, but below the overall average when it comes to revenues. A 'reduction in demand' ranks among the top three risks identified by CFOs in both countries, whereas fears about increasing labour costs and other input costs are not. CFOs in these countries do not yet expect shortages in the availability of skilled labour and so see room for an improvement in margins.

Finally, expectations of CFOs in the UK and (to a lesser extent) in Denmark are below the GDP-weighted average with respect to both revenues and margins. CFOs in Denmark are concerned about revenues – a reduction in demand is the top risk they identify – and CFOs in the UK are concerned about the weak competitiveness of the national economy.

Chart 4.1. Revenues and margins by country (%)
In your view, how are revenues/margins for your company likely to change over the next 12 months?*

GDP-weighted average net balance for revenues: 59%
GDP-weighted average net balance for operating margins: 24%



* Note: In the UK, CFOs were asked, "How are revenues/margins for UK corporates likely to change over the next 12 months?"

Data has been standardised around the (weighted) average. Bubbles on the left (right) of the vertical axis represent countries where the net balance of expectations on margins are below (above) the overall average. Bubbles above (below) the horizontal axis represent countries where the net balance of expectations on revenues are above (below) the average.

Expectations for revenues and margins vary across industries

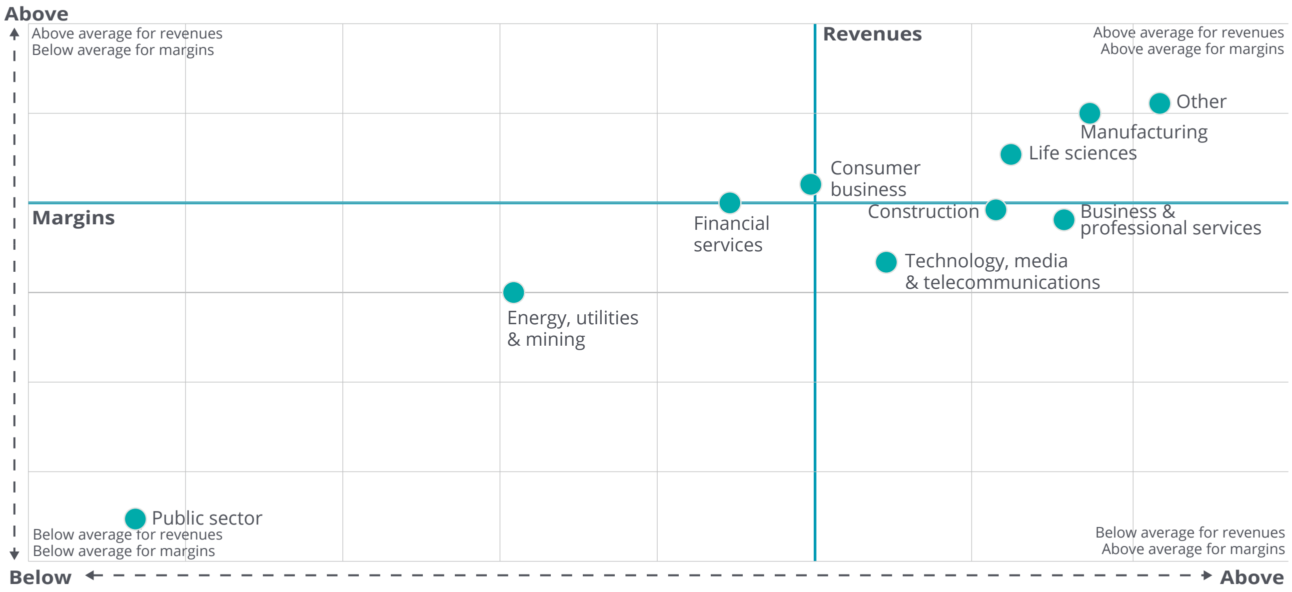
There are differences in CFOs' expectations for revenues and profit margins according to industry. CFOs in manufacturing have the most optimistic expectations about revenues. The first half of 2017 has seen sustained manufacturing activity and the global manufacturing purchasing managers' index suggests this is set to continue in the second half of the year. The fact that expectations about profit margins are above the overall average is an indication of the high levels of efficiency that are being reached in manufacturing, putting downward pressure on costs.

In the TMT sector, revenue expectations are below average: CFOs do not expect demand to pick up, so their focus is on improving efficiency. Among CFOs representing companies within the energy and resources sector, the outlook of CFOs is gloomy, with no expectations of revenue increases, efficiency gains or improvements in profit margins. In financial services, the expectations of CFOs are close to overall average for revenues, but slightly below for margins. Years of low interest rates have dented profit margins in the sector, and despite an expectation that rates will increase, this increase will not be big enough to affect expectations about margins.

Chart 4.2. Revenues and margins by industry (%)

In your view, how are revenues/margins for your company likely to change over the next 12 months?

GDP-weighted average net balance for revenues 59%
GDP-weighted average net balance for operating margins 24%

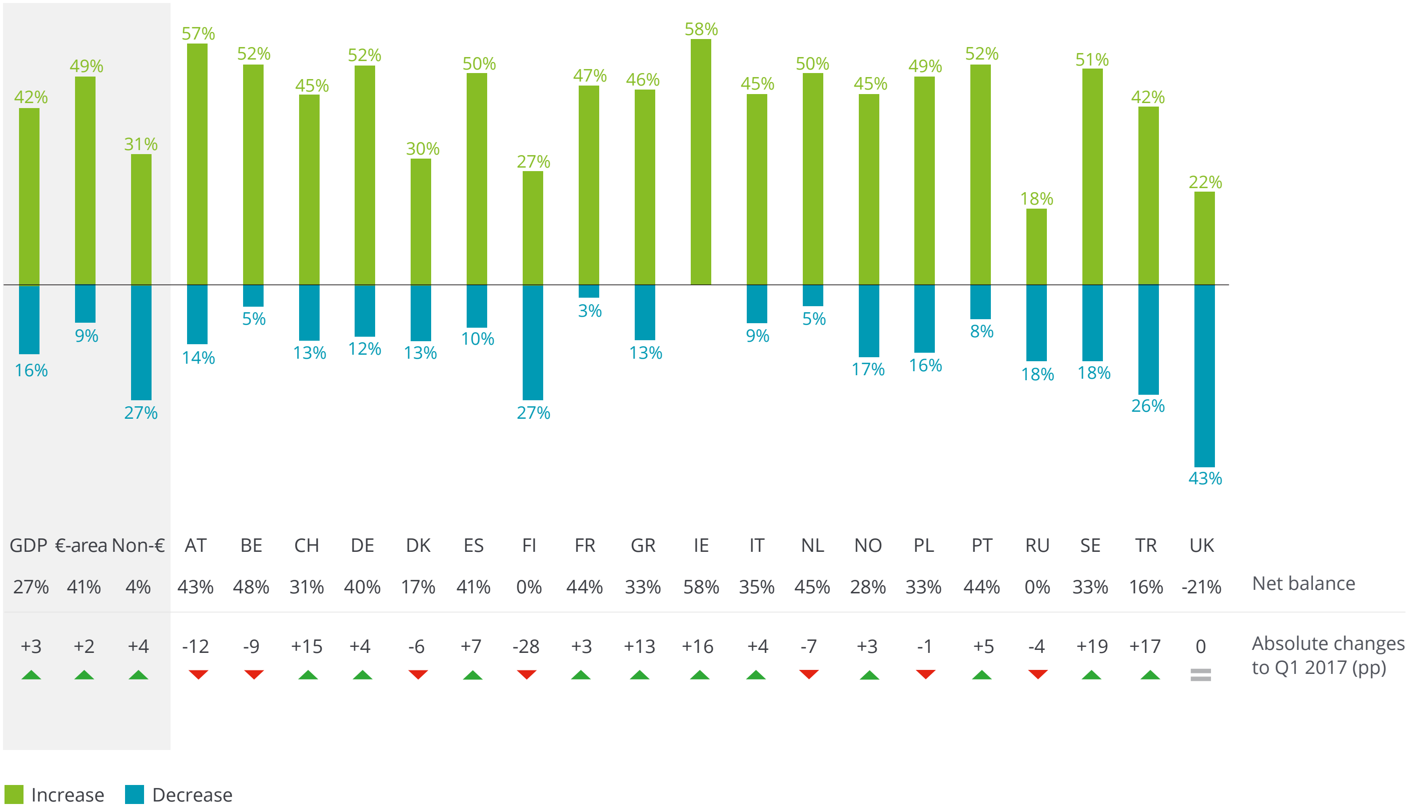


Data has been standardised around the (weighted) average. Bubbles on the left (right) of the vertical axis represent the industries where the net balance of expectations on margins are below (above) the overall average. Bubbles above (below) the horizontal axis represent industries where the net balance of expectations on revenues are above (below) the average.

CAPEX intentions increase a little

The outlook for capital expenditures (CAPEX) this quarter remains broadly positive and substantially unchanged since Q1 2017. Among CFOs across Europe, there is a net balance of +27% planning to increase capital expenditure over the next 12 months, up by 3pp since Q1 2017. While the proportion of CFOs expecting to reduce capital expenditures is exactly the same as in the previous survey, the percentage expecting an increase rose slightly. This indicates that more companies are moving towards an expansion of their business capacity.

Chart 4.3. Capital expenditure (%)
In your view, how are capital expenditures for your company likely to change over the next 12 months?*
GDP-weighted average net balance 27%



*Note: In the UK CFOs were asked "How is capital expenditure for UK corporates likely to change over the next 12 months?"

CAPEX intentions outside the euro area are much lower

Expectations about CAPEX are positive both within and (although much lower) outside the euro area. Whereas a net balance of +41% of CFOs in the euro area expect an increase in their capital expenditures, the net balance outside the euro area is only +4%. This difference is due mainly to the UK, where 43% of CFOs expect a reduction in capital expenditure by UK corporates. Business investment in the UK has been weak since the financial crisis and CAPEX expectations on average have been negative since the Brexit vote (see the Q3 2016 European CFO Survey) – although they have improved and the net balance is currently 29pp greater than in Q3 2016.

In neighbouring Ireland, on the other hand, the proportion of CFOs planning to increase their capital expenditures is the highest in the survey. With the Irish economy projected to grow, driven by robust domestic demand and a tightening labour market, CFOs seem willing to invest further.

CAPEX intentions have increased in Germany for the fourth survey in a row, with a net balance of +40% of CFOs planning to expand capital expenditure compared to those intending a reduction. This is an improvement of 18pp compared to two years ago (Q3 2015) – one of the biggest improvements within the euro area. Since the financial crisis, capital investment in Germany has been much lower than expected, so the intentions of CFOs in this area may point to a change, which would be welcome news.

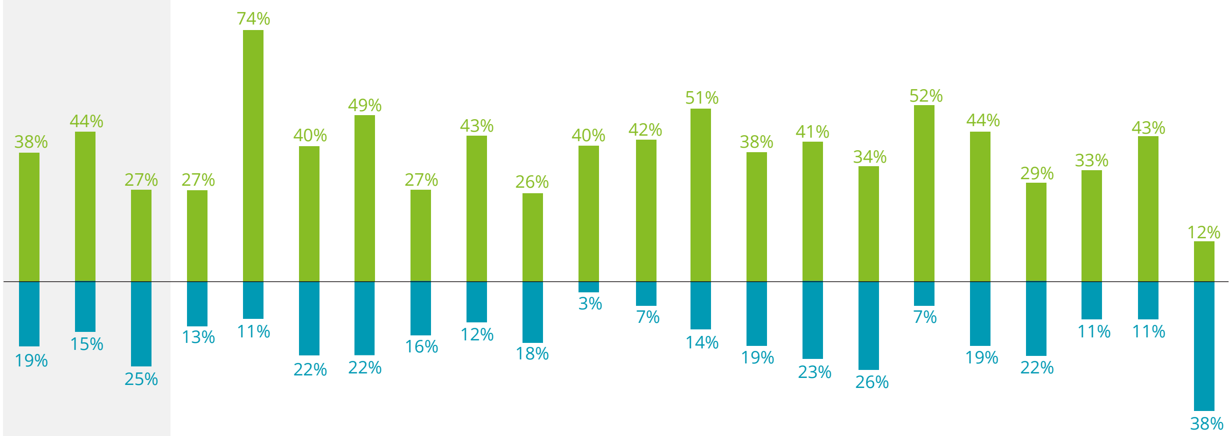
Medium-size businesses are slightly more bullish about CAPEX intentions

Responses show differences in intentions between CFOs according to the size of their business. Intentions to increase capital expenditure are greater among smaller companies than large ones, even if by a small amount. Medium-size businesses stand out as the boldest, with a net balance +30% of CFOs planning to increase capital expenditure, whereas this number for larger businesses is +25%. The focus that SMEs are putting on investment is perhaps natural, given the need to remain competitive in the face of challenges such as globalisation, digitisation and an aging population.

Companies in the euro area on the lookout for talent

As with other indicators of sentiment, the outlook on employment among European CFOs improved this quarter, with 38% of CFOs expecting employee numbers to increase over the next 12 months – the highest level since the beginning of the series. At the same time the proportion of CFOs expecting to reduce employee numbers fell to +19% – again the lowest value in the series so far.

Chart 4.4. Number of employees (%)
In your view, how is the number of employees for your company likely to change over the next 12 months?*
GDP-weighted average net balance 19%



	GDP	€-area	Non-€	AT	BE	CH	DE	DK	ES	FI	FR	GR	IE	IT	NL	NO	PL	PT	RU	SE	TR	UK
Net balance	19%	29%	2%	13%	63%	18%	27%	11%	31%	9%	38%	35%	37%	19%	18%	8%	45%	25%	7%	22%	32%	-26%
Absolute changes to Q1 2017 (pp)	+8	+10	+4	-4	+12	+1	+9	-2	+1	+9	+15	+18	-25	+17	+18	+1	+6	+8	-3	+4	+31	+2

Increase Decrease

*Note: In the UK CFOs were asked "How is the outlook for hiring for UK corporates likely to change over the next 12 months?"
In Finland the question specified a six-month period.

When comparing responses of CFOs from countries inside and outside the euro area, a similar pattern emerges to what we have already observed across other metrics – the outlook is more positive in euro area countries. The difference is substantial: for euro area countries the net balance is +29% while for countries outside the euro area it is +2%. Again the UK is the main reason for this difference.

Employment expectations are higher where unemployment is high

Changes in net balances between Q1 2017 and Q3 2017 follow the same pattern (euro area +10pp and non-euro area +4pp). Although Turkey shows the biggest improvement in net balance (+ 31pp), changes in the views of CFOs in other countries outside the euro area are more modest, probably because unemployment rates are already low. The situation is different among euro area countries, where the labour market is not as tight and CFOs have an option to expand their payroll. Indeed, the biggest improvement in the outlook for employment can be seen in Greece (+18pp), Italy (+17pp) and France (+15pp), where the unemployment rate is still high. That said, the net balance also increased markedly in Germany (+9pp), despite the unemployment rate being at its lowest level in three decades.

CFOs in manufacturing and in small businesses expect the biggest increase in hiring

The positive outlook for hiring is strongest amongst CFOs in the manufacturing industry. Financial services is the only sector where a reduction in staff numbers is expected. Expectations about hiring staff over the next 12 months are much greater among SMEs than among large companies. While a net balance of +27% of CFOs in small businesses and +21% in medium-size enterprises plan to increase the number of employees, the net balance in large companies is just +10%. These hiring intentions of CFOs suggest that there is tough competition among SMEs to attract the best talent.

Perceptions of the biggest risks are changing

Chart 5. Business risk next 12 months
Which of the following factors are likely to pose a significant risk to your business over the next 12 months?

AT
1 Skilled labour shortage
2 Labour costs
3 Increase in domestic regulations

BE
1 Competitive position in the market
2 Euro exchange rate
2 Impact of domestic financial and economic regulation

CH
1 Currency risks
2 Internal company problems
3 Geopolitical risks

DE
1 Geopolitical risks
2 Skilled labour shortage
3 Exchange rate risks

DK
1 Reduction in demand (foreign or domestic)
2 Economic outlook/growth
3 Increase in regulations

ES
1 Skilled labour shortage
2 Margin deterioration due to cost pressures
3 Margin deterioration due to lack of flexibility in pricing

FI
1 Economic outlook/growth
2 Skilled labour shortage
3 Increase in regulations

FR
1 European economic uncertainty
2 European tax and social regulations
3 Euro exchange rate

GR
1 Economic outlook/growth
2 Geopolitical risks
3 Reduction in demand (foreign or domestic)

IE
1 Geopolitical risks
2 Economic outlook/growth
3 Currency fluctuations

IT
1 Increase or change in regulations
2 Reduction in domestic demand
3 Political uncertainty

NL
1 Skilled labour shortage
2 Geopolitical risks
2 Increase in domestic regulations

NO
1 Reduction in domestic demand
2 Political uncertainty
3 Reduction in foreign demand

PL
1 Skilled labour shortage
2 Increase in costs of running a business
3 Market pressure for price decrease of offered goods/services

PT
1 Domestic regulation
2 Geopolitical risks
3 Labour costs

RU
1 Reduction in domestic demand
2 Strong competition in the market
3 Economic outlook/growth

SE
1 Reduction in demand (foreign or domestic)
2 Fierce competition/pricing power
3 Skilled labour shortage

TR
1 Weakness/strength/volatility of currency (e.g. Turkish lira)
2 Geopolitical risks
3 Deterioration of cash flow

UK
1 Effects of Brexit
2 Reduction in domestic demand
3 The prospect of higher interest rates and a general tightening of monetary conditions in the UK and US

Since Q1 2017 there has been a shift in perceptions amongst CFOs about the biggest risks facing their organisation. Among the significant risks their business will face over the next 12 months, concerns about external risks (those risks that cannot be easily managed by counter measures) appear to be easing. For example, 'geopolitical risks' feature among the top three risks for CFOs in seven out of 19 countries in Q3 2017, when in Q1 2017 it was a top three risk in ten countries. Risks linked to falling demand are also less prominent: these are still a top three risk in one-third of the countries, but this is down from 40% of countries in Q1 2015.

Risks that are more local in nature, such as those connected with work, are gaining prominence. The risk of a 'skilled labour shortage' is now a top three risk for CFOs in seven countries – three more than in the previous quarter. Labour costs, which have not featured as a prominent risk in the past, are also a concern: for the first time it is a top three risk for CFOs in two countries.

These changing perceptions of key risks confirm and reinforce the upbeat sentiment among CFOs across Europe about the medium term, but underlying long term trends may also be at work, shaping concerns about labour costs and potential skill shortages. With the population in Europe continuing to get older, finding and retaining qualified workers will be an increasing challenge. To counter this trend, CFOs are aware of the need for a strategic shift – from compensation packages to offers of training and flexible working environments.

Some shift from a defensive to an expansionary mind-set

Chart 6. Strategic priorities next 12 months
Please state to what degree the following strategies are likely to be a priority for your business over the next 12 months.

Country	Rank	Priority
AT	1	Organic growth
AT	2	Hire new talents
AT	3	Reduce costs
BE	1	Organic growth
BE	1	Control costs
BE	1	Hire new talent
CH	1	Control costs
CH	2	Organic growth
CH	3	Reduce costs
DE	1	Reduce costs
DE	2	New products/services
DE	3	Increase cash flow
DK	1	Control costs
DK	2	Reduce costs
DK	3	New products/services
ES	1	Increase productivity
ES	2	Organic growth
ES	3	New products/ services; Costs reduction
FI	1	Organic growth
FI	2	New products/services
FI	3	Reduce costs
FR	1	Reduce costs
FR	2	Expansion by acquisition
FR	3	Organic growth
GR	1	Organic growth
GR	2	Reduce costs
GR	3	Digitalisation
IE	1	Organic growth
IE	2	Control costs
IE	3	Optimise balance sheet
IT	1	New products/services
IT	2	Reduce costs
IT	3	Expand by acquisition
NL	1	New products/services or expand into new markets
NL	2	Reduce costs
NL	3	Increase capital expenditure (CAPEX)
NO	1	Organic growth
NO	2	Reduce costs
NO	3	Focus on core business
PL	1	Organic growth
PL	2	Expand by acquisition
PL	2	New products/services
PT	1	Control costs
PT	2	Working capital efficiency
PT	3	Reduce costs
RU	1	Control costs
RU	2	Organic growth
RU	3	Reduce costs
SE	1	New products/services
SE	2	Reduce costs
SE	2	Expand by acquisition
TR	1	Expand by acquisition
TR	2	Organic growth
TR	3	Increase capital expenditure (CAPEX)
UK	1	Reduce costs
UK	2	New products/services or expand into new markets
UK	3	Increase cash flow

Defensive strategy Expansionary strategy

The brighter economic outlook and the lessening uncertainty are evident in responses by CFOs to a question about the strategies that their business is likely to prioritise over the next 12 months. Expansionary strategies are on the rise. Among their top three most likely strategies, expansionary strategies outnumber defensive ones in 11 of the 19 countries in the survey, whereas just six months ago this was the case in only eight.

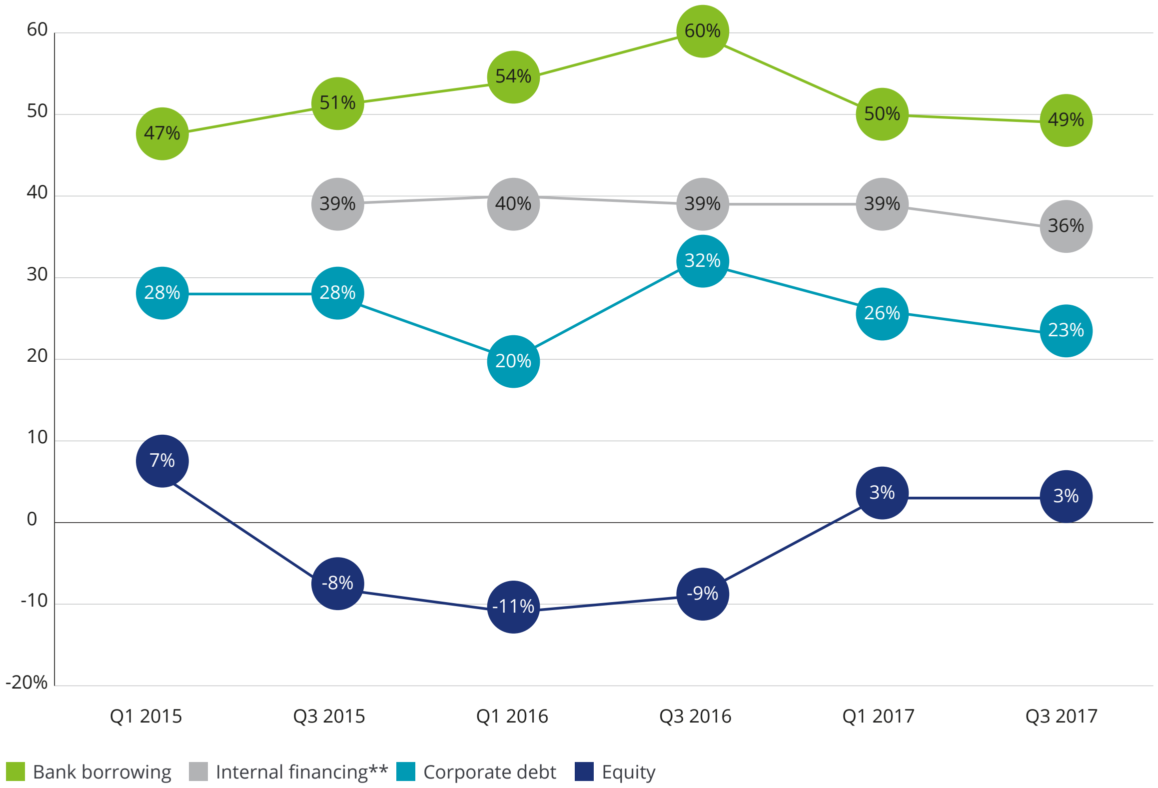
The number of countries in which the top strategic priority is a defensive one has also fallen. The majority of CFOs in eight countries identified a defensive strategy as their first priority, whereas in Q1 2017 the number was 11. The most commonly-cited defensive strategy is taking measures to 'control costs', and the most common expansionary strategy is finding ways to foster 'organic growth'.

Interestingly, digitisation is increasingly being seen as a priority business strategy. In Q1 2017, it was among the top five strategic priorities for CFOs in just one country: in Q3 2017 the number of countries has risen to four – and ranking among the top three in Greece. This is another indication that the improved economic outlook may be persuading CFOs to focus more on longer-term issues.

Sources of funding ratings virtually unchanged

CFOs are optimistic about their revenues and operating margins, they plan to increase capital expenditure and employee numbers, and over the next 12 months they are more inclined to prioritise expansionary strategies. This suggests that in the near future there might be an increase in demand for funding. At the moment compared to Q1 2017 the sources of funding for corporates in their country as rated by CFOs are practically unchanged.

Chart 7. Sources of funding – GDP-weighted net balances (%)
How do you currently rate [bank borrowing, corporate debt, equity, internal financing] as a source of funding for corporates in your country?*



*Finland and Russia asked the question as specific to "your own company."
**Internal financing was first asked in Q3 2015.

Bank borrowing remains the preferred source of funding among CFOs, especially in the euro area. Bank borrowing receives the highest ratings from CFOs in both large and medium-size businesses (net balances of +53% and +51% respectively). For smaller businesses a net balance of only +31% of CFOs identify it as an attractive source of funding while +41% identify internal financing as the most attractive.

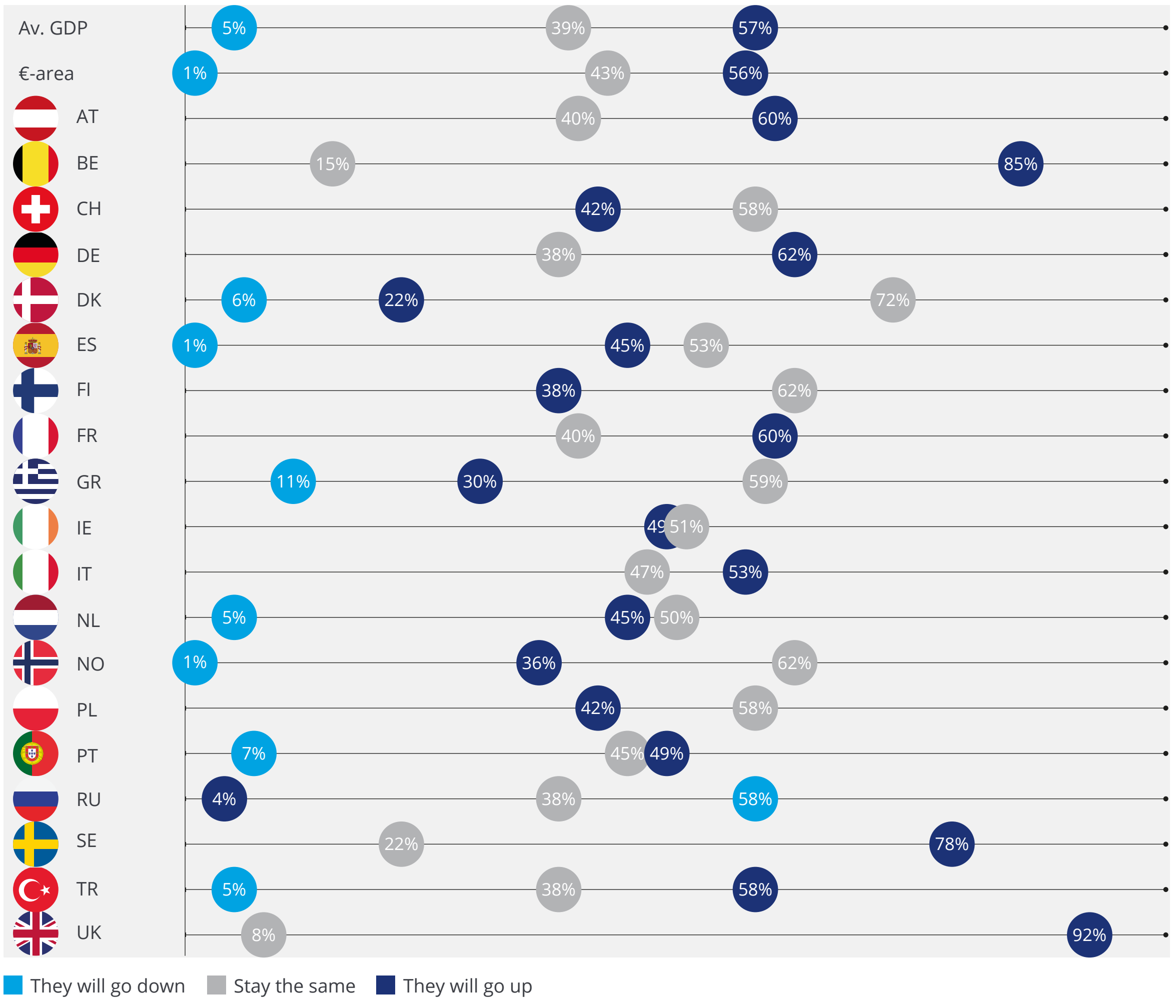
Overall internal funding is the second-best preference, although its popularity slightly declined compared to the previous quarter (-3pp). In the euro area, the net balance of CFOs who consider it a good source of funding for corporates in their country went from +37% in Q1 2017 to +33% this quarter. Outside the euro area the net balance was virtually unchanged.

Corporate debt and equity are unsurprisingly considered more attractive by CFOs in larger companies, as they are more familiar with these sources of funding for their business. For larger companies corporate debt is the second-highest rated source of funding, with a net balance of +48% while only +25% and +2% of CFOs in medium and small businesses identify it as attractive.

Interest rates expected to go up in the euro area

With the general improvement in the global economic outlook and mounting wage cost pressures, there has been growing speculation within Europe about bringing an end to years of loose monetary policies, and an increase in interest rates. A rate rise could impact company intentions around capital expenditure and hiring additional staff. We therefore asked CFOs what they expect to happen to interest rates over the next 12 months. A slight majority (+57%) consider that rates will increase.

Chart 8. Interest rate expectations next 12 months
What do you expect will happen to interest rates in your country over the next 12 months?



CFOs expectations about interest rates differ across euro area but are converging

Expectations about interest rates vary across the euro area. A majority of CFOs in Austria, Belgium, France, Italy and Germany expect rates to rise, whereas most CFOs in Greece expect no change. There seems to be a growing consensus, however, that rates will rise in the short term. The net balance of CFOs expecting some increase in interest rates over the next 12 months is +56%.

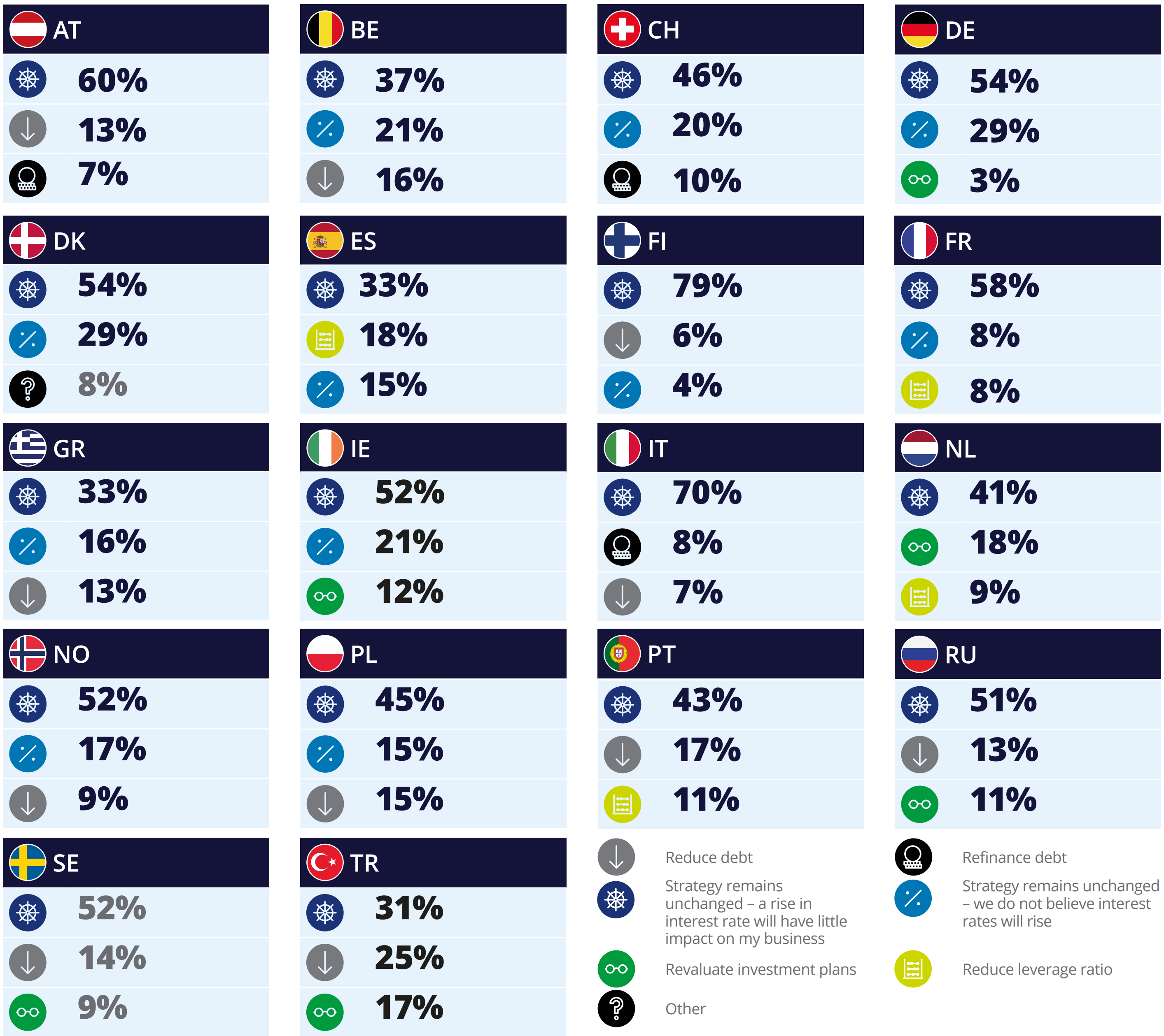
Expectations outside the euro area are mixed, driven by the country's macroeconomic situation

Outside the euro area expectations vary according to the economic situation in the country. In Russia, where monetary policy is fairly tight and the rate of inflation is falling, a majority of CFOs expect interest rates to fall. In the UK, where the rate of inflation is rising and has recently hit its highest level since 2012, CFOs largely anticipated the rate rise that was announced by the Bank of England in early November. In Switzerland, where the Swiss franc remains strong despite some depreciation recently, a majority of CFOs expect no change in interest rates.

Changes in interest rates too small to affect strategies

We asked CFOs about the strategy they would put in place, in the event of a rise in interest rates. A majority of CFOs do not expect any significant effect on their business in the event of a rise in interest rates, and so would not expect any need for their business to change its current strategies. Markets expect only a gradual rise in rates over the next year, which will probably have relatively small consequences for business. For companies in countries that could be adversely affected by a rate rise, strategies may already be in place to protect them from the potential risks.

Chart 9. Preferred strategy in the case of interest rate rise
If interest rates were to rise in the next 12 months, which one of the the following strategies do you think is most appropriate for your business?



However, some CFOs responded that their financing strategy would change, with most pointing to a reduction in their leverage ratio (9%) or an overall reduction in debt (8%). Responses did not vary substantially between industrial sectors: debt reduction would be a favoured strategy among CFOs in the energy, utilities and mining sector and in consumer businesses. CFOs in the financial services sector, unsurprisingly, would expect a re-assessment of their investment intentions.

Data summary

	GDP	€-area	Non-€	AT	BE	CH	DE	DK	ES	FI	FR	GR	IE
Compared to three/six months ago, how do you feel about the financial prospects for your company?													
More optimistic	43%	46%	**38%**	62%	48%	34%	32%	28%	48%	75%	78%	51%	56%
Broadly unchanged	45%	46%	**44%**	38%	52%	59%	56%	65%	44%	23%	19%	44%	30%
Less optimistic	11%	8%	**17%**	0%	0%	7%	12%	8%	8%	2%	3%	6%	14%
Net Balance	32%	38%	**21%**	62%	48%	27%	20%	20%	40%	73%	75%	45%	42%
How are the following key metrics for your company likely to evolve over the next 12 months?													
Revenues													
Increase	69%	73%	**63%**	77%	95%	79%	79%	47%	69%	89%	64%	76%	81%
No change	20%	19%	**22%**	23%	5%	5%	13%	35%	23%	7%	29%	16%	14%
Decrease	11%	8%	**15%**	0%	0%	15%	8%	18%	8%	4%	7%	8%	5%
Net balance	59%	65%	**48%**	77%	95%	64%	71%	29%	61%	86%	57%	68%	77%
Operating margins													
Increase	45%	49%	**39%**	27%	80%	41%	46%	40%	48%	73%	39%	35%	33%
No change	34%	37%	**28%**	67%	20%	30%	36%	41%	41%	21%	47%	52%	51%
Decrease	21%	14%	**33%**	7%	0%	29%	18%	19%	11%	5%	14%	13%	16%
Net balance	24%	35%	**6%**	20%	80%	13%	29%	21%	37%	68%	25%	21%	16%
Capital expenditure (CAPEX)													
Increase	42%	49%	**31%**	57%	52%	45%	52%	30%	50%	27%	47%	46%	58%
No change	42%	42%	**41%**	29%	43%	42%	36%	57%	40%	46%	50%	41%	42%
Decrease	16%	9%	**27%**	14%	5%	13%	12%	13%	10%	27%	3%	13%	0%
Net Balance	27%	41%	**4%**	43%	48%	31%	40%	17%	41%	0%	44%	33%	58%
Number of employees													
Increase	38%	44%	**27%**	27%	74%	40%	49%	27%	43%	26%	40%	42%	51%
No change	44%	41%	**48%**	60%	16%	38%	29%	57%	45%	56%	57%	51%	35%
Decrease	19%	15%	**25%**	13%	11%	22%	22%	16%	12%	18%	3%	7%	14%
Net Balance	19%	29%	**2%**	13%	63%	18%	27%	11%	31%	9%	38%	35%	37%
How would you rate the overall level of external financial and economic uncertainty facing your business?													
High level of uncertainty	52%	49%	**57%**	0%	24%	49%	77%	19%	30%	14%	53%	78%	51%
Normal level of uncertainty	39%	42%	**35%**	60%	52%	44%	22%	59%	50%	75%	42%	17%	44%
Low level of uncertainty	9%	9%	**8%**	40%	24%	7%	1%	23%	20%	11%	6%	5%	5%
Net Balance	44%	40%	**49%**	-40%	0%	42%	76%	-4%	10%	4%	47%	74%	47%
Is this a good time to be taking greater risk onto your balance sheet?													
Yes	33%	36%	**28%**	40%	52%	39%	25%	32%	50%	63%	36%	24%	40%
No	67%	64%	**72%**	60%	48%	61%	75%	68%	50%	38%	64%	76%	60%
Net Balance	-33%	-27%	**-43%**	-20%	5%	-23%	-51%	-37%	1%	25%	-28%	-52%	-21%
How do you currently rate [bank borrowing, corporate debt, equity, internal financing] as a source of (external) funding for corporates / your company?													
Bank borrowing													
Attractive	63%	63%	**63%**	93%	60%	65%	68%	42%	81%	56%	69%	26%	36%
Neither attractive nor unattractive	24%	27%	**18%**	7%	40%	23%	26%	45%	10%	26%	28%	46%	50%
Unattractive	14%	10%	**19%**	0%	0%	12%	6%	13%	9%	19%	3%	28%	14%
Net Balance	49%	52%	**43%**	93%	60%	54%	63%	29%	72%	37%	67%	-2%	21%
Corporate debt													
Attractive	45%	44%	**48%**	67%	55%	40%	46%	23%	58%	56%	43%	35%	43%
Neither attractive nor unattractive	32%	35%	**28%**	17%	45%	40%	42%	59%	24%	30%	47%	41%	45%
Unattractive	22%	21%	**24%**	17%	0%	20%	12%	18%	18%	15%	10%	24%	12%
Net Balance	23%	23%	**23%**	50%	55%	20%	34%	5%	40%	41%	33%	11%	31%
Equity													
Attractive	29%	28%	**32%**	55%	32%	40%	37%	14%	33%	13%	21%	34%	17%
Neither attractive nor unattractive	45%	49%	**37%**	27%	63%	44%	54%	64%	39%	48%	75%	36%	62%
Unattractive	26%	23%	**31%**	18%	5%	16%	9%	21%	28%	39%	4%	30%	21%
Net Balance	3%	4%	**1%**	36%	26%	24%	28%	-7%	4%	-26%	17%	4%	-5%
Internal financing													
Attractive	51%	47%	**61%**	67%	37%	65%	60%	57%	54%	43%	33%	53%	45%
Neither attractive nor unattractive	35%	39%	**25%**	33%	58%	27%	36%	37%	33%	41%	54%	38%	48%
Unattractive	14%	14%	**15%**	0%	5%	8%	4%	6%	13%	17%	13%	9%	7%
Net Balance	36%	33%	**46%**	67%	32%	56%	57%	50%	41%	26%	21%	44%	38%

To facilitate interpretation, this table contains a full breakdown of net balances for each question. Because of rounding, percentages may not always add up to 100.

IT	NL	NO	PL	PT	RU	SE	TR	UK
28%	23%	46%	43%	62%	53%	54%	44%	26%
64%	64%	41%	40%	30%	38%	43%	32%	47%
8%	14%	13%	17%	8%	9%	2%	24%	26%
20%	9%	32%	26%	54%	44%	52%	20%	0%
65%	77%	74%	70%	77%	60%	87%	73%	51%
22%	18%	18%	22%	12%	31%	11%	15%	25%
14%	5%	8%	8%	11%	9%	2%	13%	24%
51%	73%	66%	62%	66%	51%	84%	60%	28%
61%	68%	48%	53%	42%	60%	61%	63%	12%
27%	14%	36%	31%	35%	27%	36%	20%	27%
12%	18%	16%	15%	24%	13%	2%	17%	61%
49%	50%	32%	38%	18%	47%	59%	46%	-50%
45%	50%	45%	49%	52%	18%	51%	42%	22%
46%	45%	38%	35%	40%	64%	31%	33%	34%
9%	5%	17%	16%	8%	18%	18%	26%	43%
35%	45%	28%	33%	44%	0%	33%	16%	-21%
38%	41%	34%	52%	44%	29%	33%	43%	12%
43%	36%	41%	41%	37%	49%	57%	45%	49%
19%	23%	26%	7%	19%	22%	11%	11%	38%
19%	18%	8%	45%	25%	7%	22%	32%	-26%
16%	67%	15%	20%	48%	44%	22%	70%	85%
66%	33%	65%	53%	47%	42%	69%	27%	15%
18%	0%	19%	27%	5%	13%	9%	2%	0%
-1%	67%	-4%	-7%	42%	31%	13%	68%	85%
35%	55%	28%	34%	35%	40%	27%	14%	23%
65%	45%	72%	66%	65%	60%	73%	86%	77%
-30%	9%	-44%	-33%	-30%	-20%	-47%	-71%	-53%
38%	55%	66%	60%	57%	43%	64%	27%	86%
38%	18%	27%	28%	30%	18%	23%	18%	9%
24%	27%	7%	12%	13%	39%	14%	55%	5%
14%	27%	59%	49%	44%	4%	50%	-27%	80%
20%	50%	53%	15%	49%	20%	58%	16%	80%
14%	32%	29%	66%	40%	24%	33%	29%	14%
66%	18%	17%	19%	11%	56%	9%	55%	6%
-46%	32%	36%	-3%	38%	-36%	49%	-39%	73%
5%	41%	48%	17%	35%	13%	14%	53%	39%
15%	50%	40%	64%	45%	20%	58%	26%	34%
80%	9%	12%	19%	20%	67%	28%	22%	27%
-74%	32%	36%	-1%	15%	-53%	-14%	31%	12%
34%	N/A	N/A	64%	59%	69%	52%	49%	N/A
22%	N/A	N/A	24%	32%	13%	40%	27%	N/A
45%	N/A	N/A	12%	9%	18%	7%	24%	N/A
-11%	N/A	N/A	52%	51%	51%	45%	25%	N/A

Data summary (continued)

	GDP	€-area	Non-€	AT	BE	CH	DE	DK	ES	FI	FR	GR	IE
What do you expect will happen to interest rates in your country over the next 12 months?													
They will go up	57%	56%	57%	60%	85%	42%	62%	22%	45%	38%	60%	30%	49%
Stay the same	39%	43%	32%	40%	15%	58%	38%	72%	53%	62%	40%	59%	51%
They will go down	5%	1%	11%	0%	0%	0%	0%	6%	1%	0%	0%	11%	0%
If interest rates were to rise in the next 12 months, which one of the the following strategies do you think is most appropriate for your business?													
Reduce debt	8%	6%	14%	13%	16%	6%	4%	2%	10%	6%	4%	13%	5%
Increase debt	1%	1%	0%	0%	0%	0%	1%	1%	1%	0%	4%	1%	0%
Refinance debt	5%	5%	6%	7%	5%	10%	1%	2%	9%	4%	4%	11%	0%
Reduce leverage ratio	9%	10%	6%	7%	5%	10%	14%	0%	18%	2%	8%	8%	2%
Revaluate investment plans	8%	7%	9%	7%	11%	2%	6%	3%	5%	4%	7%	7%	12%
Adapt production plans to cope with changes in demand	2%	1%	4%	0%	0%	2%	2%	1%	1%	2%	0%	3%	0%
Shift marketing approach (e.g. less emphasis on pricing and more on other aspects)	2%	2%	2%	0%	5%	2%	1%	1%	1%	0%	3%	2%	0%
Strategy remains unchanged – a rise in interest rate will have little impact on my business	50%	52%	46%	60%	37%	46%	47%	54%	33%	79%	58%	33%	52%
Strategy remains unchanged – we do not believe interest rates will rise	12%	13%	9%	7%	21%	20%	23%	29%	15%	4%	8%	16%	21%
Other	3%	3%	4%	0%	0%	1%	1%	8%	6%	0%	3%	5%	7%

IT	NL	NO	PL	PT	RU	SE	TR	UK
53%	45%	36%	42%	49%	4%	78%	58%	92%
47%	50%	62%	58%	45%	38%	22%	38%	8%
0%	5%	1%	0%	7%	58%	0%	5%	0%
7%	5%	9%	15%	17%	13%	14%	25%	N/A
0%	0%	1%	1%	0%	0%	0%	0%	N/A
8%	5%	4%	2%	10%	7%	2%	6%	N/A
5%	9%	3%	2%	11%	4%	9%	9%	N/A
4%	18%	7%	8%	7%	11%	9%	17%	N/A
0%	0%	2%	2%	1%	9%	0%	5%	N/A
3%	9%	0%	3%	2%	0%	0%	6%	N/A
70%	41%	52%	45%	43%	51%	52%	31%	N/A
0%	9%	17%	15%	9%	0%	5%	2%	N/A
3%	5%	3%	5%	0%	4%	9%	0%	N/A

To facilitate interpretation, this table contains a full breakdown of net balances for each question. Because of rounding, percentages may not always add up to 100.

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