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CFO Signals™

What leading CFOs are thinking and doing.

2Q19 Highlights: Investing through an expected (mild) downturn

- CFOs' views on the future performance of the North American, European, and Chinese economies hit multi-year lows.
- Own-company optimism declined to the second-lowest level in the last three years.
- Expectations for revenue, earnings, and hiring growth all declined to two-year lows, but capex growth continued to rise.
- About 80% of CFOs expect an economic downturn to be mild; they are split on whether it will be short or prolonged.
- CFOs claim substantial talent constraints, but not capital constraints or shareholder pressure to use or return cash.
- Top uses of cash are investing for growth and productivity gains, with industry differences around dividends and buybacks.
- The vast majority of CFOs say they are making focused growth investments, not spreading bets across several opportunities.
- CFOs' home markets, the US, and China were most important for growth; the importance of Canada and Mexico to US CFOs seems to have declined since we last asked in 4Q15.
- CFOs' top personal focus areas are profitability, corporate strategy, and growth; other areas vary substantially by industry.

How do you regard the status of the North American, European, and Chinese economies? Perceptions of North America declined slightly, with 79% of CFOs rating current conditions as good (down from 80%), and 24% expecting better conditions in a year (down from 28%). Perceptions of Europe slid to just 10% and 4%; China sits at 26% and 10%.

What is your perception of the capital markets? Seventy-seven percent of CFOs say debt financing is attractive (up from 70%). Equity financing attractiveness rose for both public (from 25% to 40%) and private (27% to 35%) company CFOs. Sixty-four percent say US equities are overvalued, up from 46% and similar to the levels from 2018.

Overall, what risks worry you the most? CFOs express strong concerns about the impact of US trade policy on global growth and US political turmoil. Talent is the main internal concern, with newly emerging concerns about rising labor costs.

Compared to three months ago, how do you feel about the financial prospects for your company? The net optimism index declined from last quarter's +16 to just +9 this quarter—the second-lowest reading in three years. Thirty percent of CFOs express rising optimism (32% last quarter), and 21% express declining optimism (16% last quarter).

What is your company's business focus for the next year? CFOs indicate a bias toward revenue growth over cost reduction (48% vs. 29%), investing cash over returning it (51% vs. 18%) current offerings over new ones (47% vs. 32%), and current geographies over new ones (66% vs. 13%).

How do you expect your key operating metrics to change over the next 12 months? YOY revenue growth expectations fell from 4.8% to 3.8%, earnings growth slid from 7.1% to 6.1%, and hiring fell from 2.1% to 1.9% (all sit at two-year lows). Dividend growth declined from 3.9% to 3.7%, the lowest level in two years. Capital spending rose substantially from 5.9% to 7.7%.

If the US experiences a pullback, what type of pullback do you expect? About 80% expect a downturn to be mild, and they are about split on whether that downturn will be short or prolonged.

What industry and company factors are affecting your planning? All industries expected rising industry revenue over declining, with Manufacturing lowest and Healthcare/Pharma highest. All except Technology and Retail/Wholesale claimed profitability mode over growth mode; all except Financial Services were biased toward market expansion over consolidation. Overall, companies claimed talent constraints, but not capital constraints or shareholder pressure to use/return cash.

What are your company's top uses of cash this year? Top uses revolve around investment for growth and productivity improvement. There are substantial public/private and industry differences when it comes to returning cash, paying down debt, and investing for growth versus for productivity.

Which markets will be important to your company's growth over the next five years? Predictably, CFOs ranked their home markets most important. The US ranked universally high, but the importance of Canada and Mexico to US CFOs seems to have declined since we last asked in 4Q15; China is the most important market outside North America on the whole.

What is your approach to growth investments over the next three years? The vast majority of CFOs say they are making focused growth investments instead of spreading investments across multiple opportunities; capital-constrained companies are the most likely to be avoiding major investment.

On which areas will you personally focus for the next year? Three areas comprise the top tier for CFOs' personal focus: profitability, corporate strategy, and growth. Other focus areas were substantial for particular industries.

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*Averages have been adjusted to eliminate the effects of stark outliers.