

## The Deloitte CFO Survey

### Transition deal boosts sentiment

The first quarter survey of Chief Financial Officers shows slightly firmer business confidence and an easing of Brexit concerns.

The announcement of the Brexit transition deal, on 19th March, seems to have had a positive effect on the corporate mood. 84 CFOs responded to the CFO survey before the deal was announced, 22 after. Those who answered following the announcement showed significantly higher levels of optimism and risk appetite than earlier respondents. Later respondents were also less negative about the long-term effects of Brexit. For the first time in two years, CFOs do not rate Brexit as the main risk facing their businesses. Brexit has dropped to second place, with concerns about slower UK growth now at the top of the risk league.

Such uncertainties about prospects for activity in the UK are reflected in the balance sheet strategies being pursued by large businesses. CFOs in businesses that derive most of their revenues abroad report a clear focus on expansion, especially introducing new products or services and moving into new markets. Their counterparts in businesses deriving most of their revenues from the UK are operating more defensively, with cost control as their top priority.

With the unemployment rate at a 43-year low, labour shortages are emerging in the UK economy. 31% of CFOs report that recruitment difficulties or skills shortages have increased in the last three months, with none reporting a decline.

CFOs have also brought forward their estimates for the timing of interest rate rises, with 96% expecting rates to be higher in a year's time.

Business confidence has edged up and is running not far off its long-term average. CFOs have shrugged off weakness and volatility in equity markets with perceptions of uncertainty dropping to the lowest levels since the spring of 2016, before the EU referendum.

The effect of the transition announcement on this quarter's survey results underscores the sensitivity of sentiment to developments in the Brexit negotiations. The moment of truth on Brexit is approaching. The UK government hopes to strike a deal with the EU and have it endorsed by Parliament this year. Whether it succeeds in doing so is likely to be a major driver of business confidence through the rest of the year.

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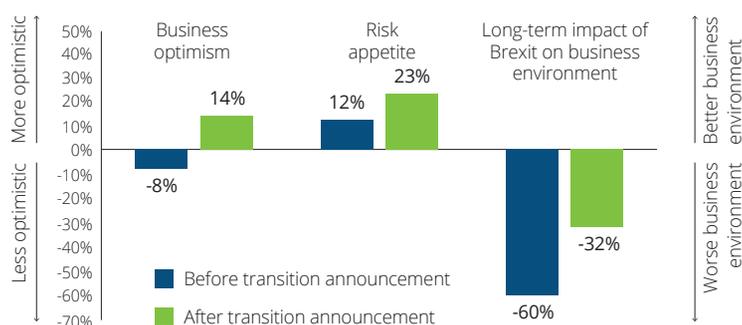
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For current and past copies of the survey, historical data and coverage of the survey in the media and elsewhere, please visit:

[www.deloitte.co.uk/cfosurvey](http://www.deloitte.co.uk/cfosurvey)

**Chart 1. Effect of Brexit transition announcement**

Net % of CFOs who are more optimistic about the financial prospects of their company now than three months ago, % of CFOs who think this is a good time to take greater risk onto their balance sheets, and net % of CFOs who think the business environment will be better/worse in the long term as a result of Brexit



# Less pessimistic on Brexit

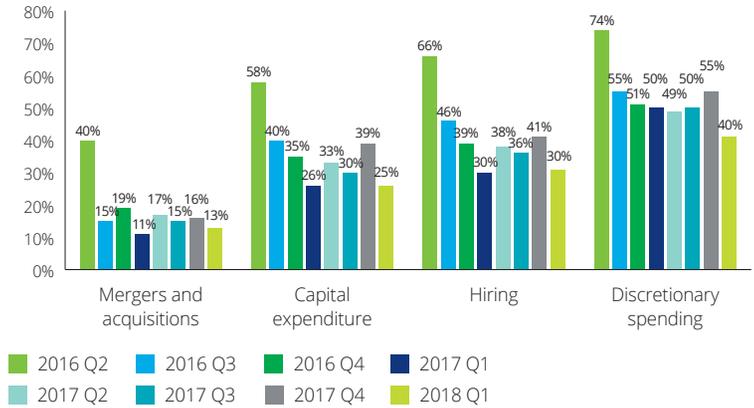
CFOs have become less pessimistic about the short-term effects of Brexit.

The proportion of CFOs who expect to reduce their own capital and discretionary spending, M&A activity and hiring, as a consequence of Brexit, are at their lowest levels in a year.

The Brexit transition announcement has had a positive effect on corporate sentiment. CFOs surveyed after the announcement were significantly less pessimistic on Brexit's impact on spending and hiring than those surveyed before.

**Chart 2. Effect of Brexit on own spending and hiring decisions**

% of CFOs who expect M&A activity, capital expenditure, hiring and discretionary spending by their business to decrease over the next three years as a consequence of Brexit



**Chart 3. Uncertainty**

% CFOs who rate the level of external financial and economic uncertainty facing their business as high or very high



CFO perceptions of uncertainty have trended down since the summer of 2016 and fell to a two-year low in the first quarter. 31% of CFOs rate current levels of external financial and economic uncertainty as high or very high.

Business optimism has edged up and is now running just below its long-term average.

**Chart 4. Business optimism**

Net % of CFOs who are more optimistic about the financial prospects of their company than three months ago



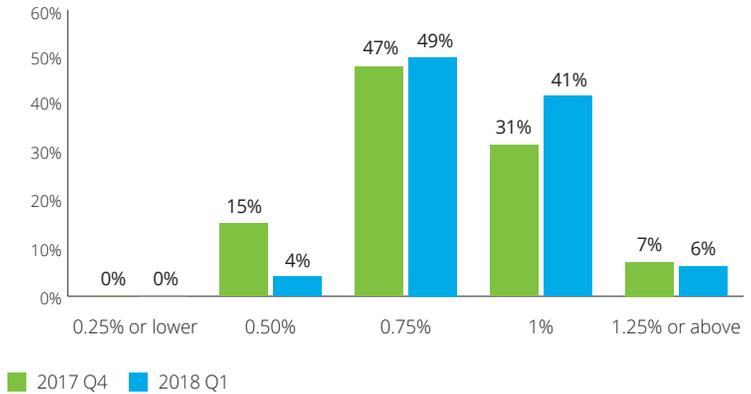
# Subdued risk appetite

CFOs see interest rate rises coming earlier than they had expected.

Almost half – 47% – expect the Bank of England’s base rate to be 1% or above, implying two 25 basis point rises, in a year’s time.

**Chart 5. Interest rate expectations**

% of CFOs who expect the Bank of England’s base rate to be at the following levels in a year’s time

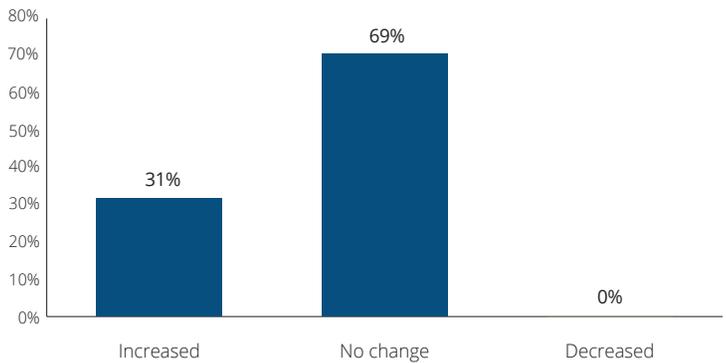


Almost a third of CFOs report that their businesses have experienced a rise in recruitment difficulties or skills shortages over the last three months.

With the unemployment rate at a 43-year low and skills shortages mounting, wage pressures seem likely to increase this year.

**Chart 6. Recruitment difficulties**

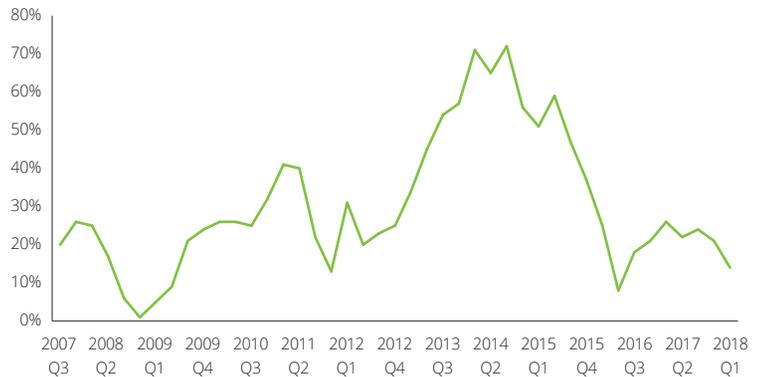
% of CFOs reporting how recruitment difficulties or skills shortages experienced by their businesses have changed over the past three months



CFO risk appetite remains subdued, declining further in the first quarter.

**Chart 7. Corporate risk appetite**

% of CFOs who think this is a good time to take greater risk onto their balance sheets

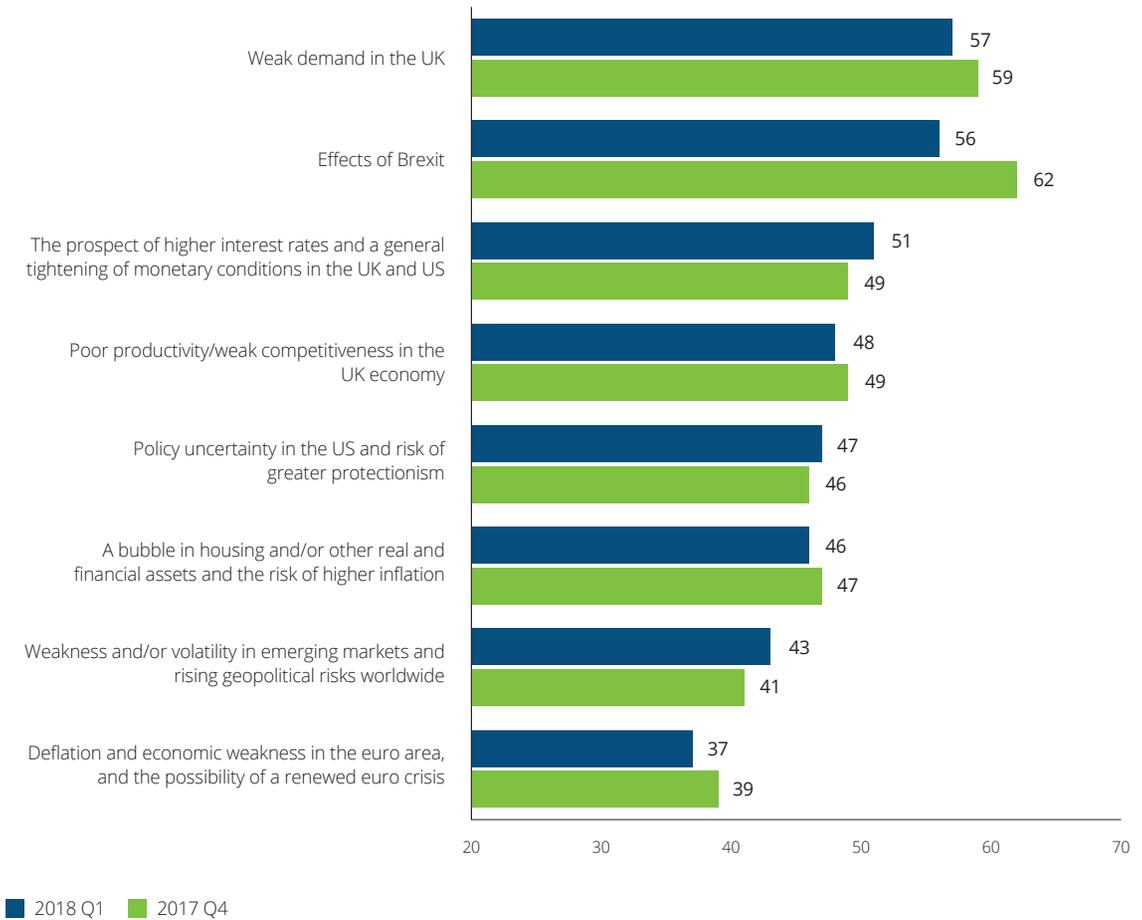


# Weak UK demand tops risk list

For the first time in two years Brexit has dropped from first position on CFOs' list of risks. Concerns around Brexit have fallen, while worries about the UK economy now top the risk list. CFOs' assessment of other risks are little-changed.

**Chart 8. Risk to business posed by the following factors**

Weighted average ratings on a scale of 0-100 where 0 stands for no risk and 100 stands for the highest possible risk



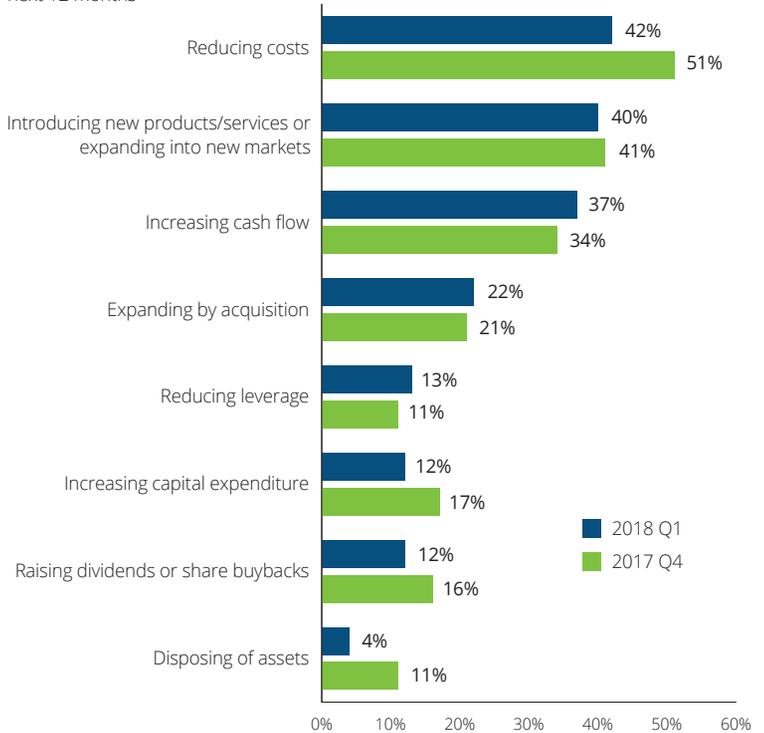
# Focus on defensive strategies

Cost reduction is the top balance sheet priority, albeit one to which CFOs attach somewhat less importance than in the fourth quarter of 2017.

Introducing new products or services or expanding into new markets ranks as the second priority followed by increasing cash flow.

**Chart 9. Corporate priorities in the next 12 months**

% of CFOs who rated each of the following as a strong priority for their business in the next 12 months



Concerns over UK demand seem to be reflected in the strategies adopted by the large corporates on our panel.

International businesses, ones that derive more than 70% of their revenues abroad, report a clear focus on expansion, especially introducing new products or services and moving into new markets. Businesses deriving most of their revenues from the UK are operating more defensively, with cost control as their top priority.

**Chart 10. Index of corporate expansion: International & UK-facing corporates**



International corporates are those that derive more than 70% of their revenues abroad while UK-facing corporates derive more than 70% of their revenues from the UK.

Difference between the arithmetic averages of the % of CFOs who rated expansionary and defensive strategies as a strong priority for their business in the next 12 months. Expansionary strategies are introducing new products/services or expanding into new markets, expanding by acquisition and increasing capital expenditure. Defensive strategies are reducing costs, reducing leverage and increasing cash flow.

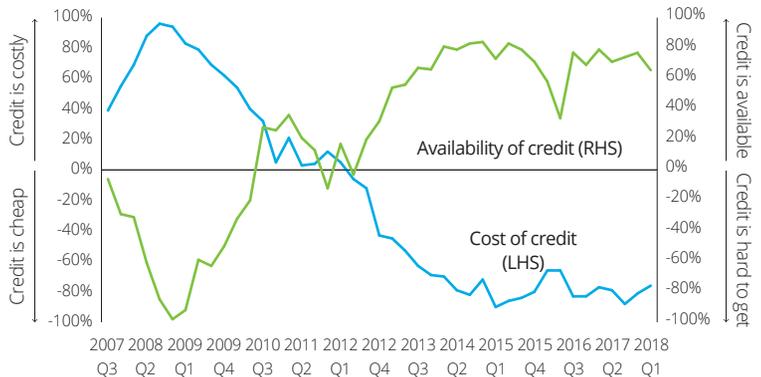
# Favourable funding conditions

The large corporates on our survey panel have easy access to credit.

CFOs continue to view credit as being easily available and close to its cheapest in ten years.

**Chart 11. Cost and availability of credit**

Net % of CFOs reporting credit is costly and credit is easily available



Debt finance – bank borrowing and bond issuance – remains the most attractive source of funding for CFOs.

Equity issuance is seen as being significantly less appealing.

**Chart 12. Favoured source of corporate funding**

Net % of CFOs reporting the following sources of funding as attractive



CFOs think that the return of cash to shareholders through share buy backs and dividends has increased and is running at high levels.

On balance, 29% of them report cash return ratios as higher than normal, the highest reading in ten years.

**Chart 13. Cash return to shareholder ratios**

Net % of CFOs who think cash return to shareholder ratios (including dividends and share buybacks) are high relative to normal levels



# CFO Survey: Economic and financial context

## The macroeconomic backdrop to the Deloitte CFO Survey Q1 2018

The International Monetary Fund revised up its global growth forecasts for 2018. Manufacturing activity accelerated in the US, the euro area, China, Japan and the UK. Unemployment continued to fall in the US and euro area, and remains at a 43-year low in the UK. In a sign that wage pressures are building, latest data shows wages in the US and UK rising at their fastest pace in eight and two-and-a-half years respectively. Equity market volatility rose in the first quarter. Treasury and gilt yields rose as investors expect further rate rises. The US Federal Reserve raised interest rates and increased its projections for future rate hikes. The Trump administration passed a bill cutting US corporation tax and introduced tariffs on metals and specific duties targeting China. In Germany, Chancellor Angela Merkel's conservative CDU party forged a coalition with the centre-left Social Democratic Party. The EU and UK announced terms for a 21-month Brexit transition period, paving the way for negotiations on a future trading relationship before the UK's departure from the EU on 29th March 2019.

### UK GDP growth: Actual and forecast (%)



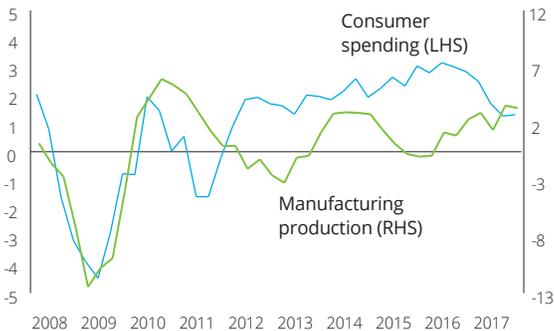
Source: ONS, Consensus Economics and Deloitte calculations

### FTSE 100 price index



Source: Thomson Reuters Datastream

### UK consumer spending and manufacturing production growth (%)



Source: Thomson Reuters Datastream

### UK annual CPI inflation (%)

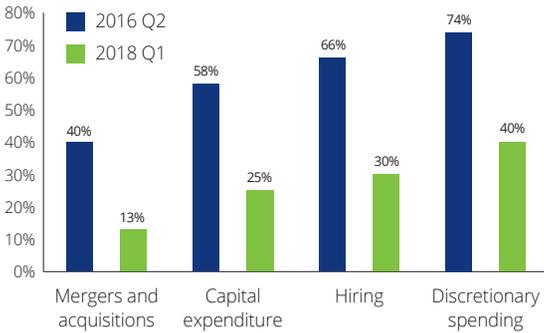


Source: Thomson Reuters Datastream

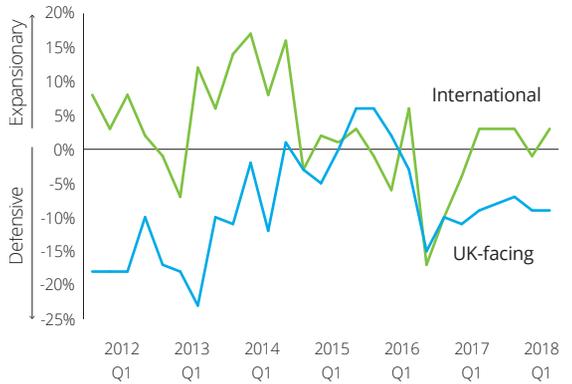
# Two-chart summary of key survey messages

## Effect of Brexit on own spending and hiring decisions

% of CFOs who expect M&A activity, capital expenditure, hiring and discretionary spending by their business to decrease over the next three years as a consequence of Brexit



## Index of corporate expansion: International & UK-facing corporates



\* Detailed definition under Chart 10. inside

### About the survey

This is the 43<sup>rd</sup> quarterly survey of Chief Financial Officers and Group Finance Directors of major companies in the UK. The 2018 first quarter survey took place between 7th and 21st March. 106 CFOs participated, including the CFOs of 24 FTSE 100 and 42 FTSE 250 companies. The rest were CFOs of other UK-listed companies, large private companies and UK subsidiaries of major companies listed overseas. 84 CFOs responded to the survey before the transition deal was announced on 19th March and 22 CFOs responded after. The combined market value of the 78 UK-listed companies surveyed is £427 billion, or approximately 17% of the UK quoted equity market.

The Deloitte CFO Survey is the only survey of major corporate users of capital that gauges attitudes to valuations, risk and financing. To join our panel of CFO respondents and for additional copies of this report, please contact Anthea Neagle on 020 7303 0116 or email [aneagle@deloitte.co.uk](mailto:aneagle@deloitte.co.uk)

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