CFO innovation ASIA

BUSINESS OUTLOOK SURVEY

THIRD QUARTER 2012

CONTENT

KEY TAKEAWAYS

CFO Innovation Asia surveyed 250 CFOs, finance directors, controllers and other senior executives across Asia from 10 to 18 July 2012. The key findings include the following:

After recovering in the previous survey, CFO optimism has plunged once again in the third quarter. Four out of ten finance executives polled (44%) now say they are less optimistic or not optimistic at all about the growth prospects of the economy where they are based, up from 32% who said the same in the second quarter.

Still, a hardy 20% express optimism (previous survey: 35%), with the remaining 36% saying they see no change (34% in the previous survey).

Confidence in company performance has also levelled off, but the fall is not as steep. Nearly a third (31%) of the executives surveyed are less optimistic/not optimistic at all about the growth prospects of their own firm, up from 27% in the previous survey. More CFOs today say their company's outlook has not changed (39%), compared with the 26% who said the same in the previous survey.

Company optimism is higher than optimism on the economy (31% versus 20%), possibly reflecting CFO confidence in their organisation's ability to survive and thrive even in a downturn, as Asian companies have demonstrated since the 1997 Asian financial crisis.

On the theory that executives have more visibility into their company's growth prospects than they do into the wider economy, and given that business growth is a key driver of GDP expansion, it may be that the prospects for the region's economies are more positive than current CFO expectations indicate.

Consistent with their comparatively sunnier outlook on their company's prospects, respondents forecast higher sales in the next 12 months. The majority – 53% – of executives expect rising sales, although this proportion is down from 60% in the previous survey. A plurality (46%) also forecast larger profits, down from 53% three months ago.

CFOs are not particularly worried about some company-level risks. Only 28% of the executives surveyed now expect receivables at risk to increase, down from 31% in the previous survey and 43% in the beginning of the year. The proportion of those forecasting a longer Days Sales Outstanding period also remains low at 26% (compared with 30% and 41%, respectively, in the previous two surveys).

But companies remain cautious on capital and other spending. Only 34% of respondents say their firm will increase capital expenditures, the same proportion as in the previous two surveys. Twenty seven percent will spend more on marketing and advertising (30% in the previous survey), while 20% will increase R&D investment (previous survey: just 16%).

The proportion of companies that will intensify M&A activity stands at 24%, an improvement from the 17% in the fourth quarter of last year.

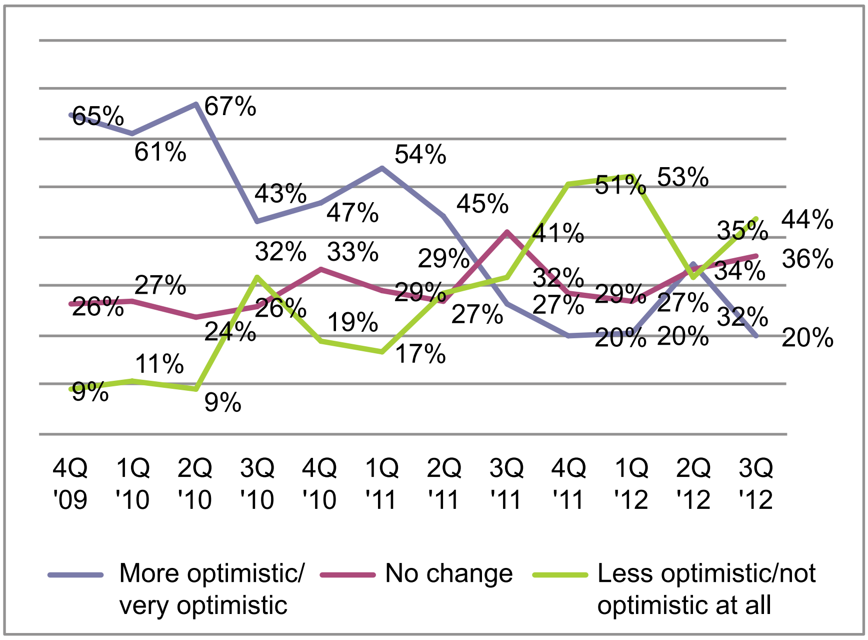
Consumer demand remains on top of the list of external concerns. It is rated as a top-three concern by 60% of respondents (previous survey: 53%), followed by currency risk (35% vs. 29% previously) and government regulations (33% vs. 32%).

Foreign competition is a rising top-three worry at 27%, up from 19% in the beginning of the year. This may be an indication of actual or expected refocusing of US and European MNCs, and Asian regional businesses, on selling to Asian consumers and businesses as the economic environment in the US and Europe continues to be volatile.

Attracting and retaining qualified employees remains the top internal concern. Half of the executives surveyed point to this as a top-three internal worry (54% in the previous survey). Cost-cutting is the second key concern (36%), followed by maintaining morale and productivity, and working capital management (both 29%).

Economic outlook: Embracing the negative

How optimistic are you about the prospects of the economy where you are based?



Base: 160 respondents (4Q 2009); 205 (1Q 2010); 215 (2Q 2010); 165 (3Q 2010); 147 (4Q 2010); 144 (1Q 2011); 119 (2Q 2011); 165 (3Q 2011); 215 (4Q 2011); 192 (1Q 2012); 286 (2Q 2012); 250 (3Q 2012). Totals may not add up to 100% due to rounding

In the previous survey, Asia's CFOs were almost equally split between optimism, pessimism and being on the fence about the outlook for the economy where they were based.

No longer. In this current survey, they have come down on the negative side. Forty four percent of the finance executives interviewed say they are less optimistic/not optimistic at all about the growth prospects of the local economy, compared with 35% who said the same previously.

A hardy 20% remains more optimistic/very optimistic, however (previous survey: 35%). The remaining 36% think the local economy will remain basically unchanged.

Renewed worries about Greece – despite the electoral victory of political parties that have endorsed a tough rescue programme – and fears about the much larger Spanish economy have dominated business news, along with the slowing pace of the Chinese economy.

While Japan and most of Southeast Asia have reported encouraging second-quarter GDP results, the respondents seem to give more weight to the negative tone of the global economic environment and the inevitable effect on Asia's economies.

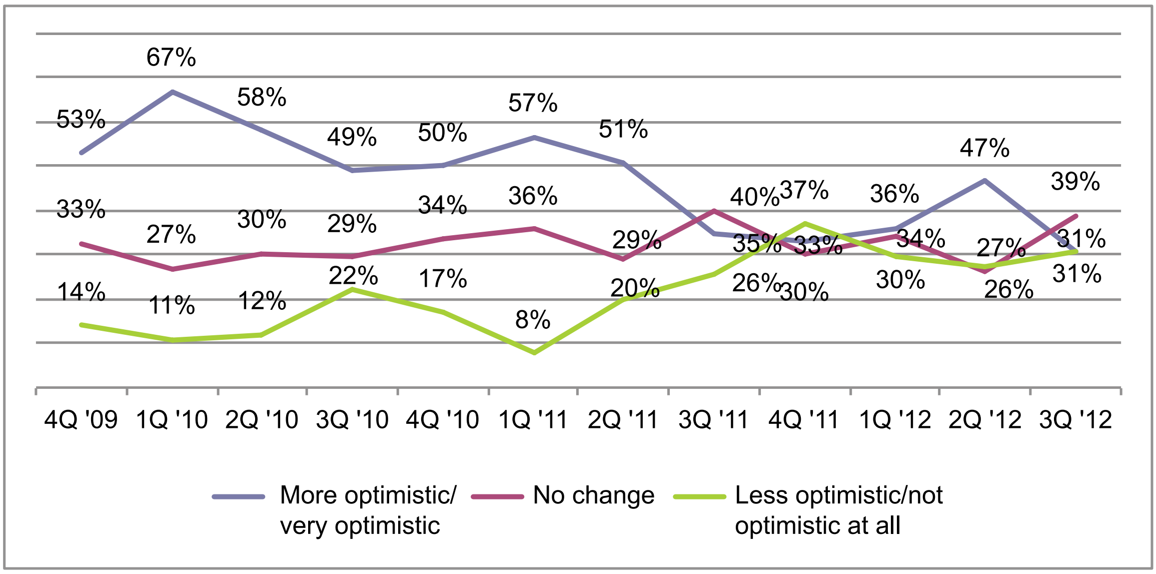
Resilience at the company level

As in the previous surveys, the proportion of respondents who are more optimistic/very optimistic about the growth prospects for their own company is higher compared with those optimistic about the economy (31% versus 20%).

The gap between macro-economic and own-company optimism stands at 11 percentage points, which is narrower than the first quarter survey's 16 percentage points.

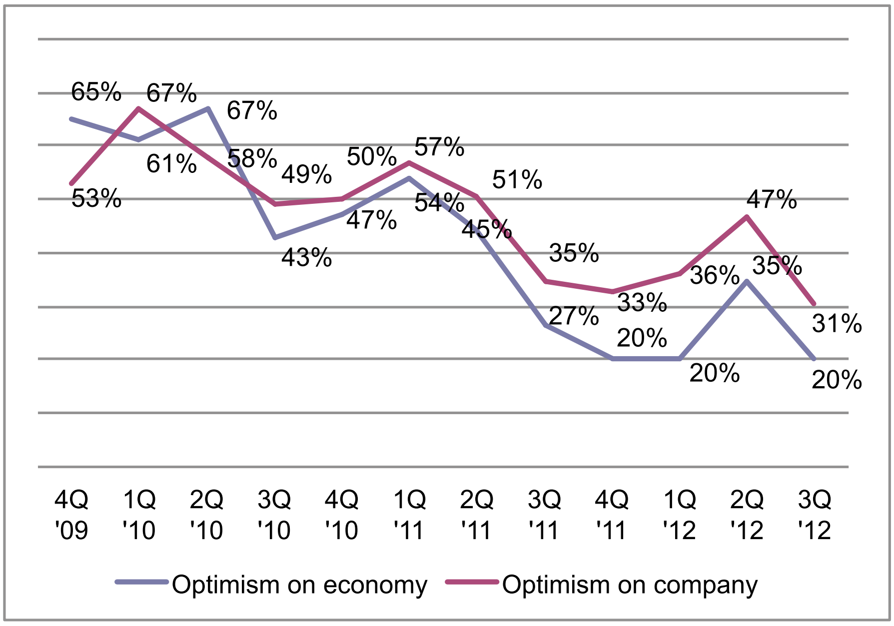
Evident since the third quarter 2010 survey, the divergence became more pronounced towards the end of last year, with respondents consistently more optimistic about their own company's prospects than they are about the local economy, as shown in the chart below.

How optimistic are you about the growth prospects of your own company?



Base: 124 respondents (4Q 2009); 202 (1Q 2010); 214 (2Q 2010); 163 (3Q 2010); 143 (4Q 2010); 143 (1Q 2011); 116 (2Q 2011); 164 (3Q 2011); 214 (4Q 2011); 188 (1Q 2012); 286 (2Q 2012; 249 (3Q 2012). Totals may not add up to 100% due to rounding

Macro-economic versus own-company optimism



Base: 116 to 286 respondents

Between these two measures, company sentiment may be the more reliable view because CFOs have more visibility into their own firm's metrics than they do into macro-economic numbers and trends.

On the theory that executives have more visibility into their company's growth prospects than they do into the wider economy, and given that business growth is a driver of GDP expansion, the prospects for Asia economies may be more positive than current CFO expectations indicate.

That said, there could be other explanations for the gap, including a belief that the company can survive and thrive regardless of how badly the local economy is doing, on the evidence of its resilience since the 1997 Asian financial crisis.

Sales and profits: Waning optimism

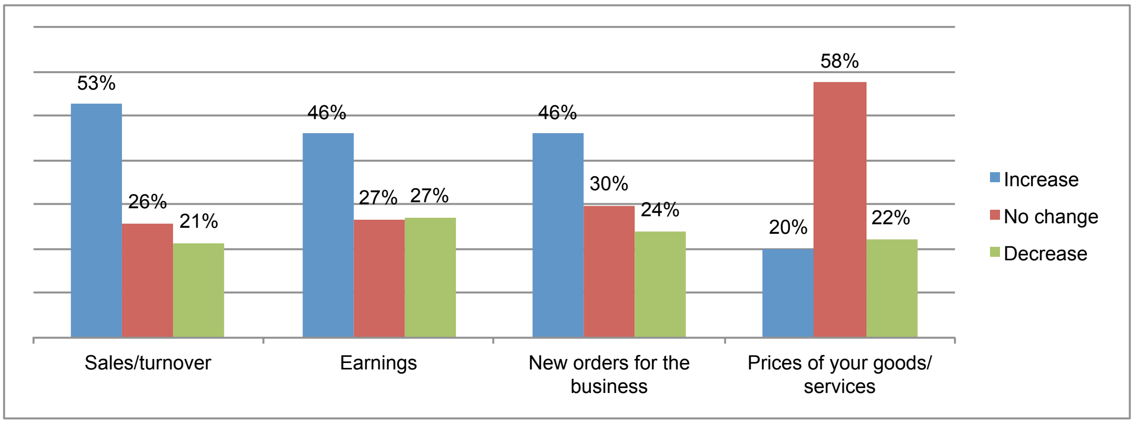
As in the previous survey, the majority of companies still expect revenues to rise in the next 12 months (53%), although the proportion is lower than the 60% of three months ago.

But optimism on profits is waning, with only 46% expecting higher earnings compared with 53% in the previous survey.

A similar plurality of executives still forecasts getting new orders for the business (46%). This is also down from the previous survey (54%), indicating expectations of (or actual experience with) slowing export orders and possibly less buoyant domestic consumption.

The proportion of those who believe their company will enjoy pricing power going forward has fallen as well, to 20% from 29% in the previous survey.

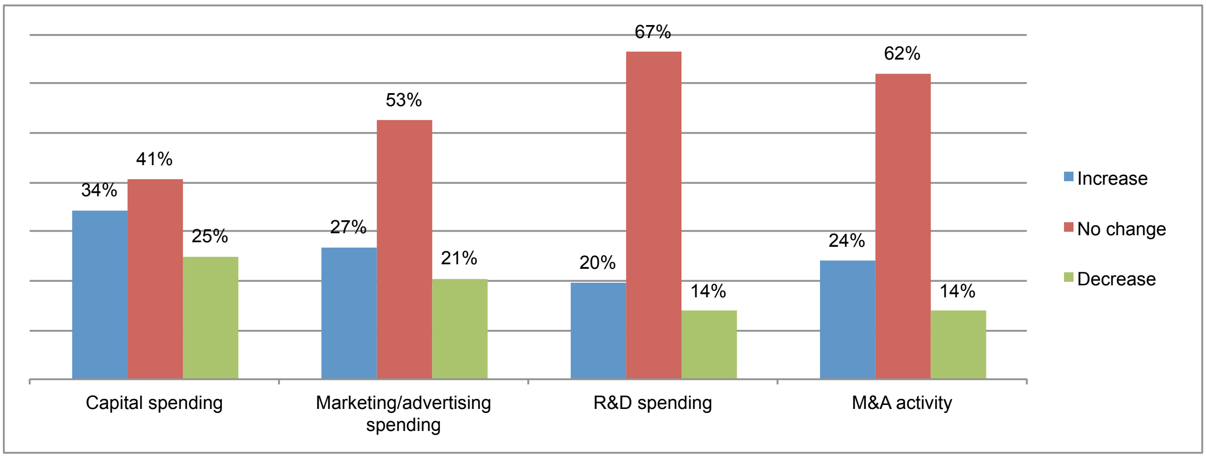
What changes does your company anticipate in the next 12 months?



Base: 224 respondents. Totals may not add up to 100% due to rounding

Holding back on capex

What changes does your company anticipate in the next 12 months?



Base: 224 respondents. Totals may not add up to 100% due to rounding

Caution in capex and other spending has been evident in the two previous surveys and this continues to be the case in this current research. The proportion of respondents who say their company will increase capital expenditures remains at 34%. Fifty one percent had planned to increase capex in the third quarter of 2011.

Twenty five percent will actually cut back on capex (previous survey: 21%), while 21% will decrease marketing/advertising spend (previous survey: 22%).

Twenty four percent of respondents expect increased M&A activity, unchanged from the previous survey but a marked improvement from the 17% who said the same in the fourth quarter last year.

Twenty percent will increase spending on research and development (previous survey: 16%). The proportion of companies in Asia that plan to increase R&D spending has never breached 30% since this survey was started in 2009, which arguably may not bode well for long-term business sustainability.

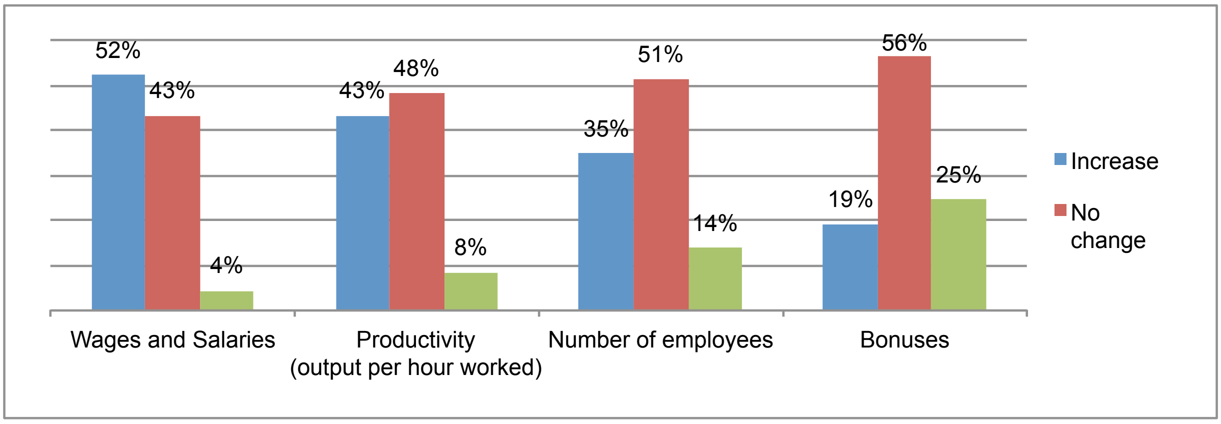
Caution on personnel

It's also status quo on personnel matters. The majority of respondents (51%) now expect employeee numbers to remain unchanged, compared with just 36% who said the same in the beginning of the year and 46% in the previous survey. And where 44% in the first quarter survey said staff numbers would increase, today only 35% expect to hire more (previous survey: 37%).

Even so, the majority of companies will still increase wages and salaries (52%), though the proportion of those doing so is now lower compared to the number in beginning of the year (69%). Bonuses will remain unchanged as well (56%) or even decreased (25%).

Perhaps because wage increases and bonuses will be curtailed, only 43% expect productivity to increase (previous survey: 52%), with 48% predicting no deterioration.

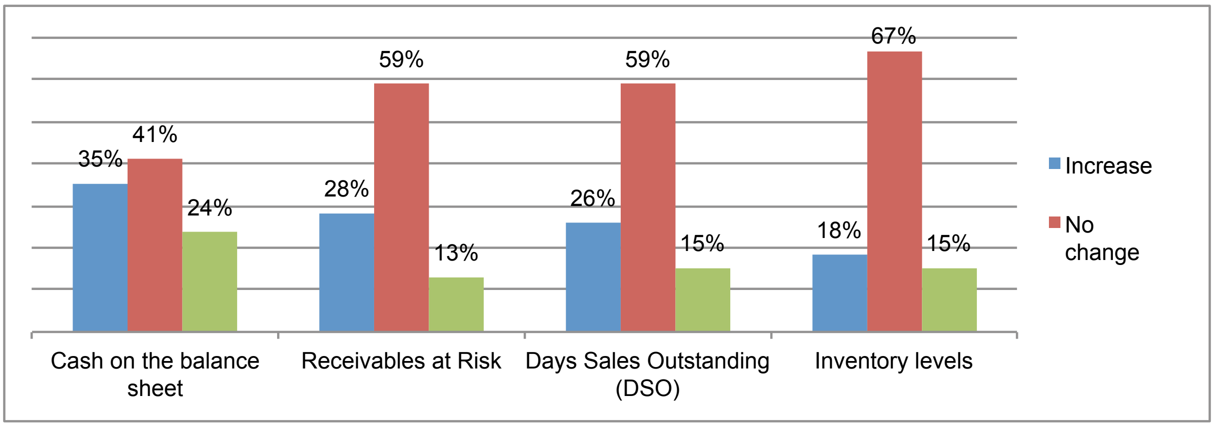
What changes does your company anticipate in the next 12 months?



Base: 224 respondents. Totals may not add up to 100% due to rounding

Cash the king

What changes does your company anticipate in the next 12 months?



Base: 224 respondents. Totals may not add up to 100% due to rounding

Consistently since this survey was started in September 2009, respondents indicate that their company will not decrease cash on the balance sheet. The proportion of enterprises that will bring down cash levels has never gone beyond 23% – until the fourth-quarter 2011 survey, when 29% said their company would decrease cash levels in the next 12 months.

This trend may be reversing. Only a quarter of respondents now say their company will decrease cash on the balance sheet, compared with 30% in the beginning of the year. This is consistent with the finding that companies are holding back on capex and other spending, as well as on wage increases and bonuses.

Thirty five percent of respondents say their company will continue accumulating cash (previous survey: 36%). Many analysts have made the point that if there is one lesson that Asian businesses have internalised from the 1997 Asian financial crisis, this is it: Cash is king.

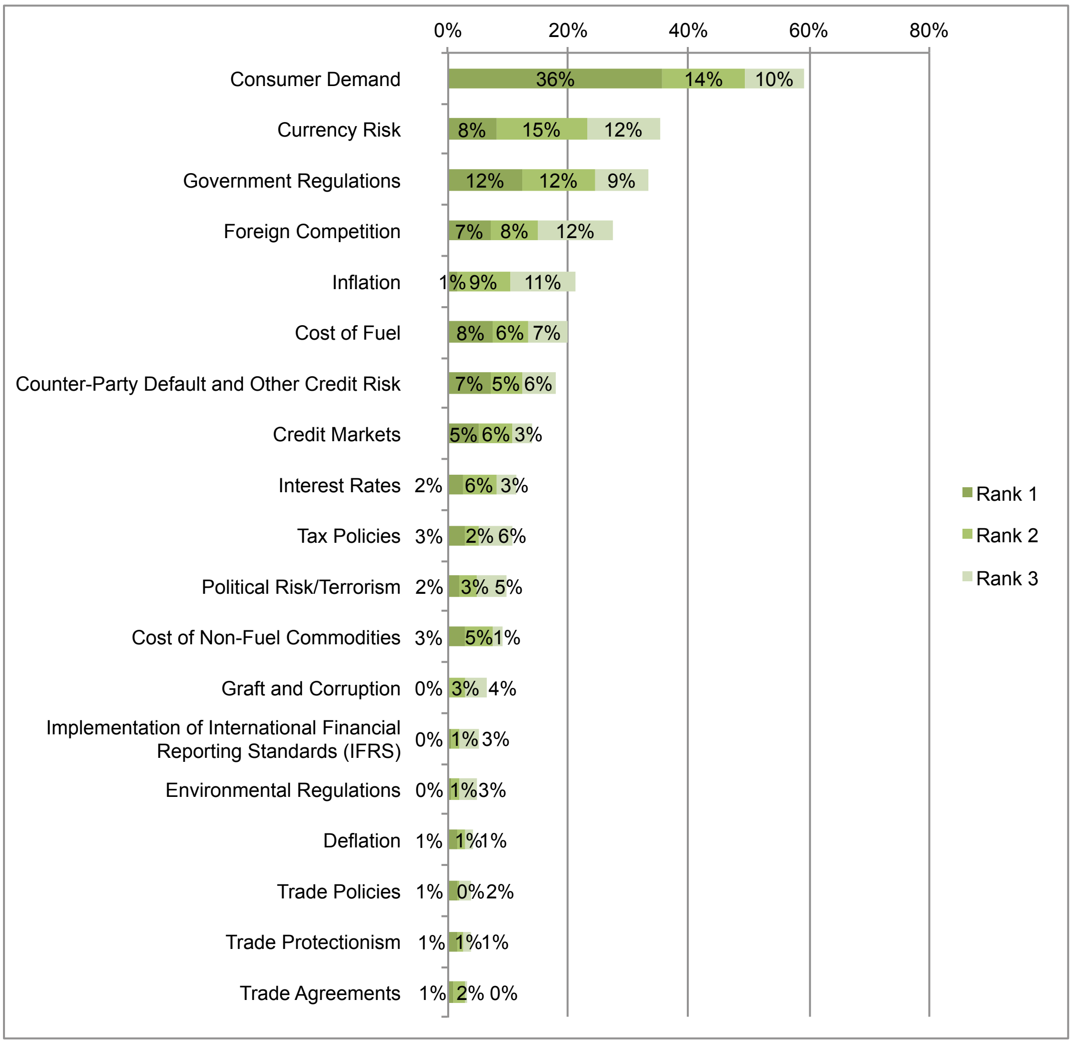
There were indications in the beginning of the year that CFOs were expecting economic stress to build up among counter-parties, a number of them presumably European buyers, given the Western orientation of Asia's exports. Those fears continue to dissipate, with only 28% of respondents seeing increased volumes of receivables at risk in their company (versus 31% in the previous survey and 43% in the beginning of the year).

This does not necessarily mean a belief that Europe's economic problems will be solved, but more likely a function of the individual company's confidence that it has cleaned up its counter-party roster and has instituted sufficient risk mitigation measures.

The proportion of those forecasting a longer Days Sales Outstanding period also remains low at 26% (compared with 30% and 41%, respectively, in the previous two surveys).

Foreign competition: Intensifying worries

What are the most serious external issues that face your company?



Base: 213 respondents.

Respondents were asked to identify and rank the top three external issues their company faces, with Rank 1 denoting the most serious concern. Consumer demand continues to be regarded as the most serious challenge, with 36% ranking it as the number one external issue (previous survey: 35%).

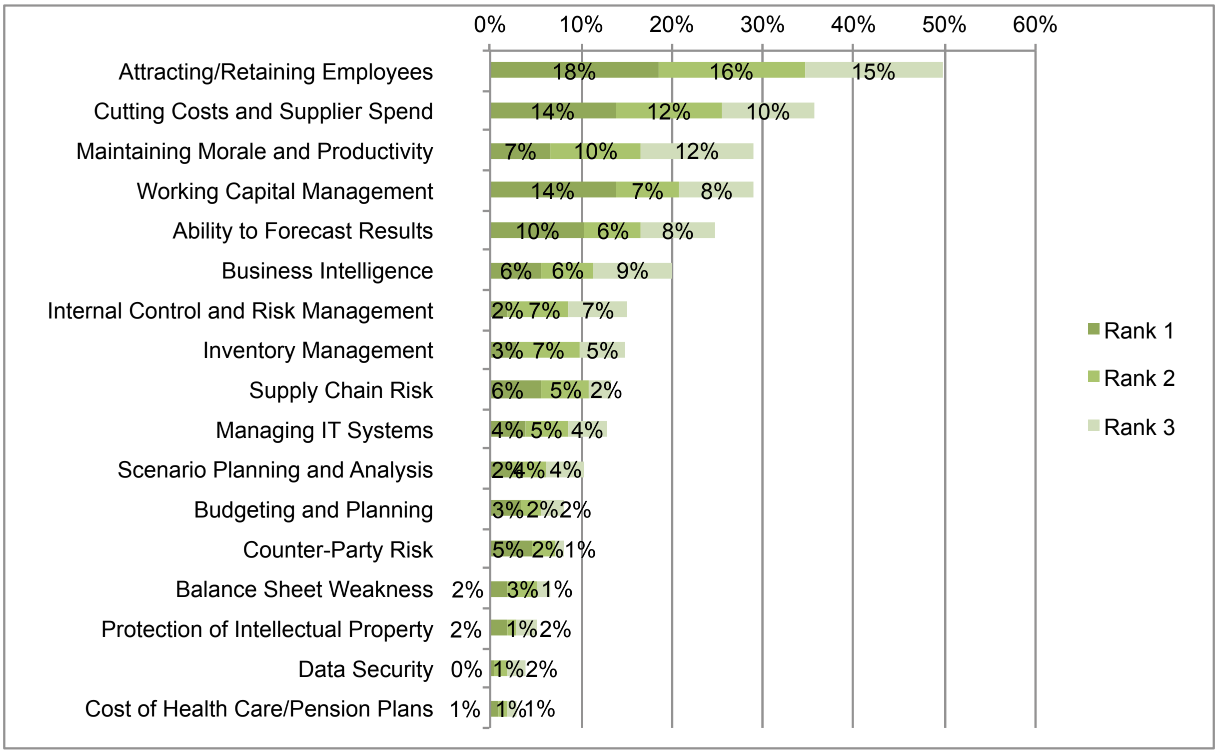
Consumer demand is a top-three concern for 60% of the executives surveyed, up from 53% in the previous survey, followed by currency risk (35% versus 29% in the previous survey) and government regulations (33% vs. 32% previously).

Inflation is falling down the list of worries, with only 1% ranking it as the No. 1 external concern compared with 9% in the beginning of the year. In the current survey, 21% cite inflation as a top-three worry (beginning of the year: 26%).

Worries about foreign competition are intensifying; 27% say it is a top-three concern (beginning of the year: 19%). Asian companies may be experiencing or expecting US and European MNCs (and regionalising Asian companies) to refocus on selling to Asian consumers and businesses as the US and Europe continue to be dogged by one crisis after another.

Keeping talent, cutting costs

What are the most serious internal issues that face your company?



Base: 211 respondents

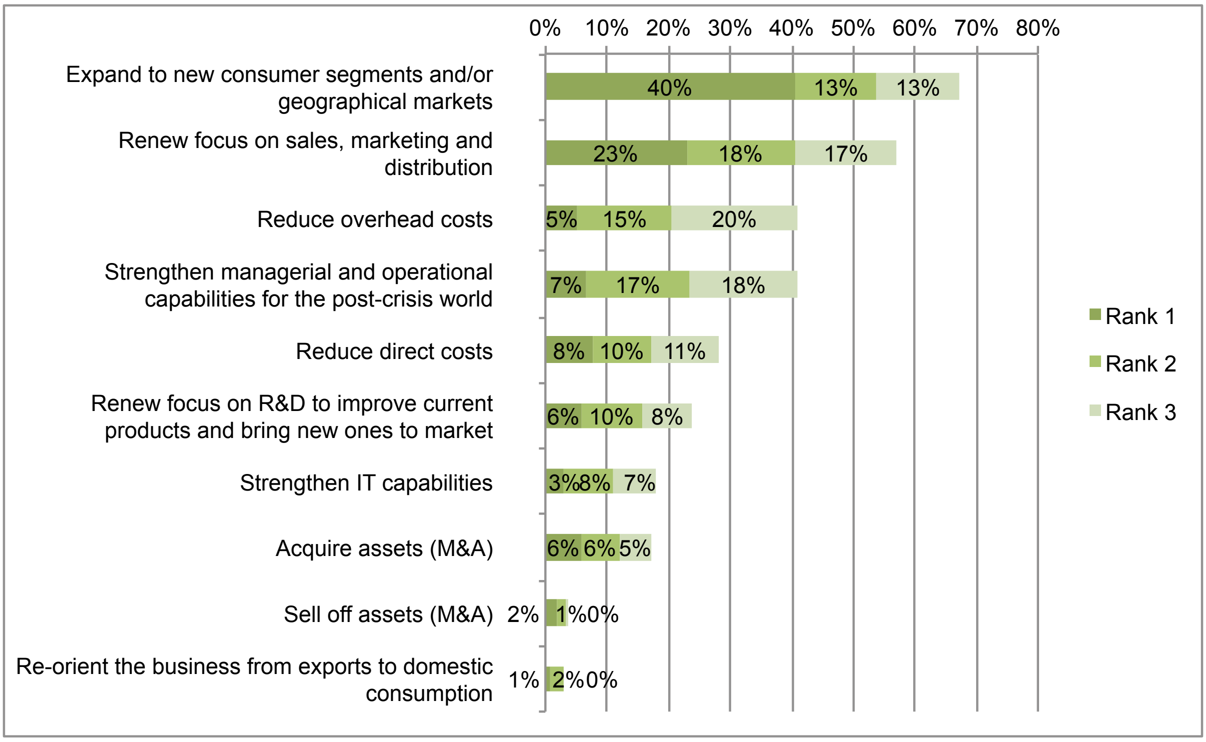
Respondents were also asked to identify and rank the top three internal issues their company faces. Attracting and retaining qualified employees is ranked the No. 1 internal challenge (18% versus 22% in the previous survey). Half of respondents cite recruitment and retention as a top-three concern (previous survey: 54%).

This is a reversal of the ranking in the first quarter 2012 survey, when the key top-three concern was cutting costs and supplier spend (46%), followed by attracting and retaining qualified employees (41%).

Still, cost management remains a significant internal concern, with 36% rating it a top-three worry (previous survey: 41%).

It’s the growth, stupid

What is your company’s strategic focus in the next 12 months?



Base: 210 respondents

The strategic focus of the executives surveyed has remained constant over the 12 iterations of this survey series: Grow the business.

In this survey, 66% of the CFOs surveyed cite expanding to new consumer segments and/or geographical markets as a top-three focus in the next 12 months (previous survey: 63%). Fifty eight percent will renew the focus on sales, marketing and distribution (57% previously).

At the same time, though, 40% cite as top-three strategic focus the reduction of overhead costs, while 29% point to reduction of direct costs.

There are risks, as there always will be, but the respondents are clearly keeping the faith. Europe and the volatile global environment may affect Asian economies and businesses, but past experience has shown that recovery can be swift.

What is needed is to strike the appropriate balance between spending for growth and cost-cutting for financial and operational efficiency, between risk-taking and risk aversion. This is the challenge facing the CFO and the finance function – and the rest of the enterprise.

About this report

Fieldwork for this online survey was conducted from 10 to 18 July 2012. Cesar Bacani, *CFO Innovation*'s Editor-in-Chief, devised the questionnaire, analysed the results, and wrote the report. Eric Lam, Art Director at Questex Asia, designed the report.

A total of 250 respondents from Singapore, Hong Kong, India, Malaysia, China and other jurisdictions in Asia participated in this survey. They are CFOs, finance directors, controllers and other senior executives who work in a range of companies in terms of turnover, employee numbers and industry.

Respondents are personally based in the following markets...

Singapore	25%
Hong Kong	19%
India	12%
China	11%
Malaysia	9%
Philippines	5%
Indonesia	5%
Australia	2%
Other	11%

Total may not add up to 100% due to rounding

...hold positions with the following titles...

CFO/Finance Director	49%
Financial controller	16%
Finance manager	8%
CEO, Chairman, President, Managing Partner or Owner	6%
Vice President Finance	3%
Other senior finance executive	4%
Other C-level executive or Partner	2%
Treasurer	1%
Other	10%

Total may not add up to 100% due to rounding

...work in companies with these employee numbers...

Fewer than 50	9%
51 to 200	21%
201 to 500	18%
501 to 2,000	26%
2,001 to 5,000	11%
More than 5,000	16%

Total may not add up to 100% due to rounding

...have the following in annual turnover...

Less than US$1 million	4%
US$1 million to US$5 million	6%
More than US$5 million to US$10 million	5%
More than US$10 million to US$20 million	9%
More than US$20 million to US$50 million	13%
More than US$50 million to US$100 million	12%
More than US$100 million to US$200 million	16%
More than US$200 million to US$500 million	10%
US$501 million to US$1 billion	8%
Over US$1 billion	19%

Total may not add up to 100% due to rounding

...and engaged in the following industries:

Manufacturing	15%
Consulting/Other professional services	11%
Electronics/software/high-tech	10%
Banking/finance/insurance	9%
Conglomerate/diversified businesses	6%
Pharmaceuticals/healthcare	6%
Fast-moving consumer goods	5%
Energy/mining	5%
Chemicals	4%
Logistics/distribution	4%
Industrial equipment	4%
Property and construction	4%
Transportation/travel/hotel	4%
Telecommunications	3%
Automotive	3%
Retail	3%
Other	3%

Total may not add up to 100% due to rounding

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