CFO innovation ASIA

BUSINESS OUTLOOK SURVEY

THIRD QUARTER 2011

CONTENT

KEY TAKEAWAYS

CFO Innovation Asia surveyed 165 CFOs, finance directors, controllers and other senior executives across Asia from 3 June to 4 July 2011. The key findings include the following:

Going into the third quarter of 2011, the recovery in economic optimism that started late last year has dissipated. Only 27% of the executives surveyed are now more optimistic or very optimistic about the growth prospects for the economy where they are based, compared with 45% in the previous survey. The proportion of business executives who are less optimistic or not optimistic at all has risen to 32%, from 29% in the previous survey, equal to the high of 32% recorded in third quarter 2010.

However, the largest proportion – 41% – say they see no change in the growth prospects of the economy where they are based, indicating a measure of confidence that the economy will not contract but will continue to grow, albeit at a slower pace.

Confidence in company performance has weakened. Just a third of respondents (35%) now say they are optimistic about the growth prospects for their own company, compared with 51% in the previous survey. This is the lowest level of optimism since this survey was launched in September 2009. The level of pessimism is also at its highest since the start of this survey, at 26%, compared with 20% in the previous survey.

Again, as in economic prospects, 40% of the executives surveyed see no change in their company's growth prospects, an indication that they expect continued growth, but not as much perhaps as in the recent past.

It seems the cautious sentiment is not yet affecting sales and earning forecasts. Six out of ten respondents (61%) still expect their company's sales to rise in the next 12 months, although fewer (50%) anticipate improved earnings. In the previous survey, 70% forecast higher sales (82% in the first quarter survey) while 56% expected better profits (65% in the first quarter survey).

Companies have not yet reached the point where they are cutting back on capital and other spending. Indeed, 51% of respondents say their company will increase capital spending (previous survey: 47%). Forty five percent will spend more on marketing and advertising, unchanged from the previous quarter. Companies remain interested in mergers and acquisition as well. The proportion of companies that will increase M&A activity is at 31% (previous survey: 29%), higher than the 17% in the fourth quarter of 2010.

Hiring intentions are moderating, however. Only 48% of respondents now expect to see higher employee numbers in the next 12 months (previous survey: 54%). But expectations that companies will still need to raise salaries to recruit and retain talent remain high – 70% are bracing for higher wages (previous quarter: 69%).

Inflation remains a key area of concern, but cost of fuel has receded somewhat in the list of worries. While consumer demand remains the No. 1 external issue, as it has been since the start of this series in 2009, inflation worries also remain prominent, a trend that was first detected in the first quarter of this year. Currency risk remains a concern as well, along with government regulations and foreign competition.

Perhaps reflecting the growing pessimism about the prospects for the local economy, reducing overhead costs is now the second most cited strategic focus in the next 12 months. This was No. 3 in the previous survey, following expansion to new consumer segments and/or geographical markets (No. 1) and renewing focus on sales, marketing and distribution (No. 2). In this survey, expanding to new segments remains the No. 1 priority, but renewing focus on sales, marketing and distribution is now No. 4.

Optimism on the economy dissipates

Going into the third quarter, the return of economic optimism in Asia that started late last year appears to have largely dissipated. Only 27% of the executives surveyed are now more optimistic or very optimistic about the growth prospects for the economy where they are based, compared with 45% in the previous survey.

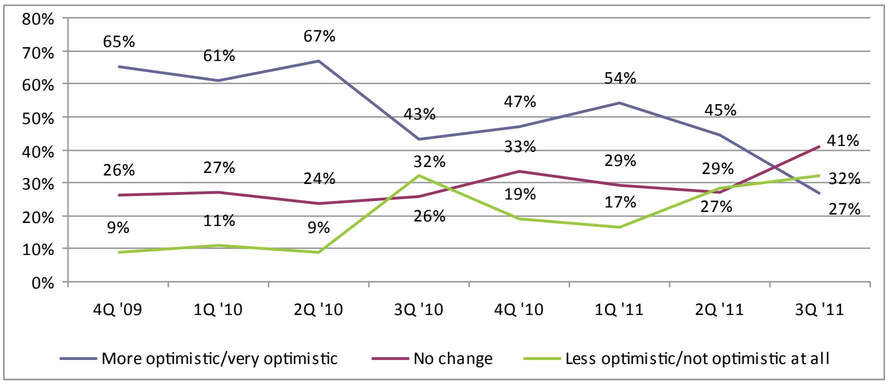
The proportion of business executives who are less optimistic or not optimistic at all has risen to 32%, from 29% in the previous survey. This equals the high of 32% recorded in third quarter 2010.

However, 41% of respondents, the largest proportion, say they see no change in the growth prospects of the economy where they are based. Since economies across most of Asia have continued to grow, albeit at a moderating pace, this indicates a measure of confidence that the region's expansion story remains intact.

Fieldwork for this survey spanned a period of rising inflation and higher interest rates in China and elsewhere in Asia, combined with negative news flow around renewed problems in Europe's periphery and the uncertain outcome of negotiations to raise the federal government's debt ceiling in the US.

Indications that China's economy is headed towards a soft landing came after the end of the fieldwork. If this positive trend continues and clarity is reached around the current uncertainties in Europe and the US, economic optimism in Asia may return, a trend we will be looking at closely in the next survey results.

Exhibit 1: How optimistic are you about the growth prospects of the economy?



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). Totals may not add up to 100% due to rounding

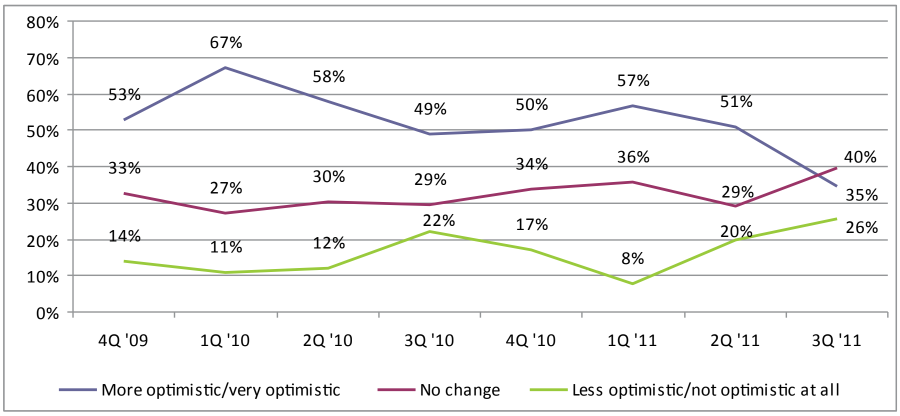
Confidence in company performance has weakened

Only a third of respondents (35%) say they are optimistic about the growth prospects for their own company, compared with 51% who made the same assessment in the previous survey. This is the lowest level of optimism since the first survey in September 2009.

The level of pessimism is also at its highest since the start of this survey, at 26%, compared with 20% in the previous survey. Very few – 8% – had been pessimistic about their company's growth prospects in first quarter 2011, an indication of how strongly inflation and interest rates, as well as the negative news flow, are affecting business sentiment.

However, as in the macro-economic picture, 40% of the executives surveyed say they see no change in their company's growth prospects. Since 51% of respondents had expressed optimism in the previous survey and 20% had been pessimistic, the large number in the 'no change' column may be regarded as, by and large, not an outright negative.

Exhibit 2: 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). Totals may not add up to 100% due to rounding

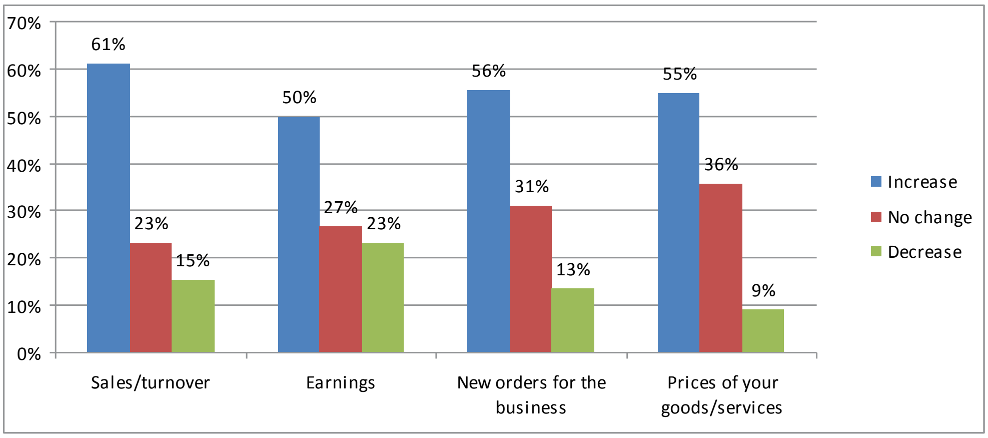
Expecting rising sales, not so much on profits

The respondents' cautious outlook has yet to be fully reflected in their sales and earnings expectations. Six out of ten respondents (61%) still expect sales to increase (previous survey: 70%) while 50% anticipate higher profits (previous survey: 56%). Although still substantial, these numbers are far below the 82% who forecast higher sales in the first quarter of the year and 76% who predicted higher earnings.

The downward trend is evident in anticipated new orders for the business as well – 56% forecast an increase, but this is down from 62% in the previous survey and 76% in the beginning of the year.

One grace note is the seeming recovery in pricing power, with 55% of respondents expecting to be able to raise the prices of their goods/services in the next 12 months, compared with 50% who said the same in the previous survey. This may be a response to inflation expectations, which is something that companies may be able to piggyback on to improve margins.

Exhibit 3: What changes does your company anticipate in the next 12 months?



Base: 142 respondents. Totals may not add up to 100% due to rounding

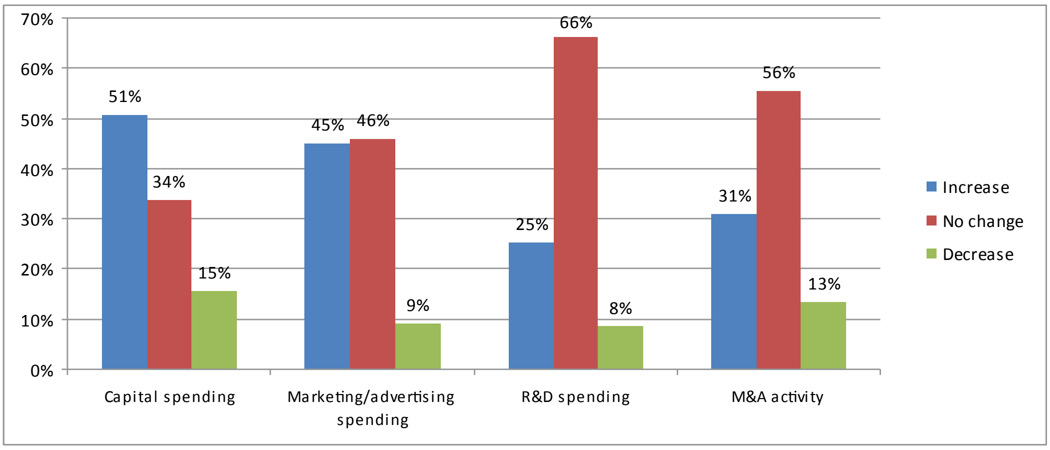
The M&A trend grows stronger

M&A activities will intensify in the next 12 months, according to 31% of respondents, up slightly from the 29% who said the same in the previous survey. This continues a rising trend that was detected for the first time in the first quarter 2011 survey, when M&A intentions rose to 31%, up from just 17% previously.

The cautious macro-economic and own-company outlook does not seem to be affecting spending plans at this time. Fifty one percent of respondents say their company will increase capital spending (previous survey: 47%). Forty five percent will intensify marketing and advertising (previous survey: 46%).

Only 25% will increase spending on research and development. The proportion of companies 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 sustainability.

Exhibit 4: What changes does your company anticipate in the next 12 months?



Base: 142 respondents. Totals may not add up to 100% due to rounding

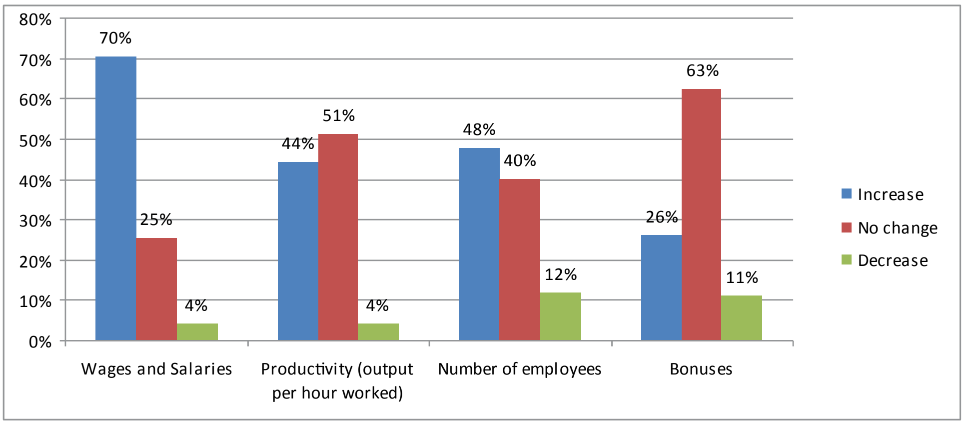
Ever higher wages, moderating hiring

Asia's companies will raise wages in the next 12 months – 70% of the executives surveyed expect salaries to increase (previous survey: 69%), although the proportion is down from 79% in the first-quarter survey.

But fewer now expect to see intensified hiring (44% versus 54% in the previous survey and 60% in the first quarter).

The proportion of respondents who expect their company to increase bonuses has also fallen to 26%, from 37% in the previous survey and 43% in the first quarter. Only 11% plan to cut bonuses, however – 63% say these payments will stay at the same levels.

Exhibit 5: What changes does your company anticipate in the next 12 months?



Base: 142 respondents. Totals may not add up to 100% due to rounding

Is cash forever the king?

Consistently since this survey was started, the executives surveyed say their company will not decrease cash on the balance sheet. The proportion of enterprises that will draw down cash levels has never gone beyond 23%. In this survey, the eighth iteration in the quarterly series, only 21% of companies will decrease cash levels in the next 12 months.

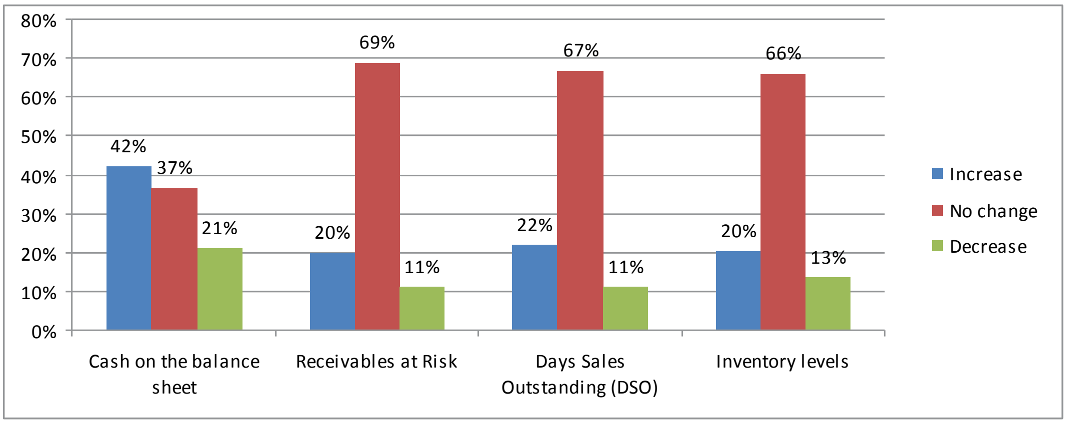
Indeed, 42% will continue to accumulate cash (previous survey: 41%), although that is down from 52% in the first quarter survey. Some analyts may judge that this is not a productive way of utilising company resources. But Asia's enterprises evidently have no intention of forgetting the key lesson of the 1997 Asian financial crisis, which was validated again during the 2008-2009 global financial crisis: Cash is king.

The region's companies continue to take a benign view of receivables at risk, with just 20% of respondents expecting risky exposures to rise (previous survey: 28%). Sixty seven percent expect risky receivables to remain at the same levels or even fall (11%).

Days sales outstanding (DSO) are also expected to remain stable (67%), with 11% of respondents saying their organisation will shorten DSO in the next 12 months. Only 22% now anticipate that DSO will deteriorate, down from 31% in the previous survey.

Fewer companies are also increasing inventory levels (20% versus 31% in the previous survey and 27% in the first quarter), possibly in anticipation of slowing consumption because of inflation and higher interest rates. Most are keeping inventory levels at the same level (66% versus 58% in the previous two surveys), rather than decreasing them (13% versus 18% in the previous survey).

Exhibit 6: What changes does your company anticipate in the next 12 months?



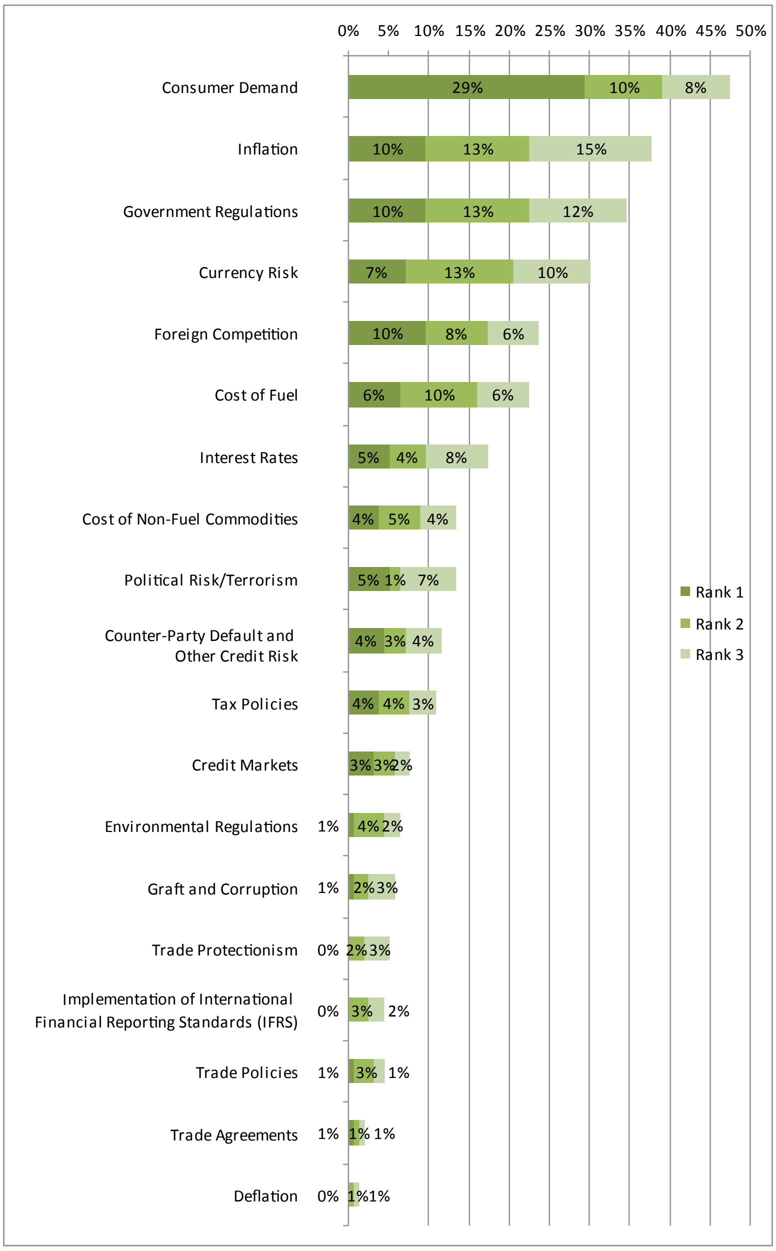
Base: 142 respondents. Totals may not add up to 100% due to rounding

Consumer demand and inflation

Respondents were asked to identify and rank the top three external issues their company faces, with Rank 1 denoting the most important. Consumer demand continues to be regarded as the most serious challenge, with 29% ranking it as the number one external issue (previous survey: 23%). It is a top-three concern for 47% of the executives surveyed, which is perhaps not surprising in an inflationary and rising interest rate environment.

The next three top-three external concerns are inflation, government regulations and currency risk, which were top of mind (except for government regulations) in the previous survey. Government moves to change or tighten rules have overtaken cost of fuel and even currency risk as a key concern.

Exhibit 7: What are the most serious external issues that face your company?



Base: 156 respondents. Totals may not add up to 100% due to rounding

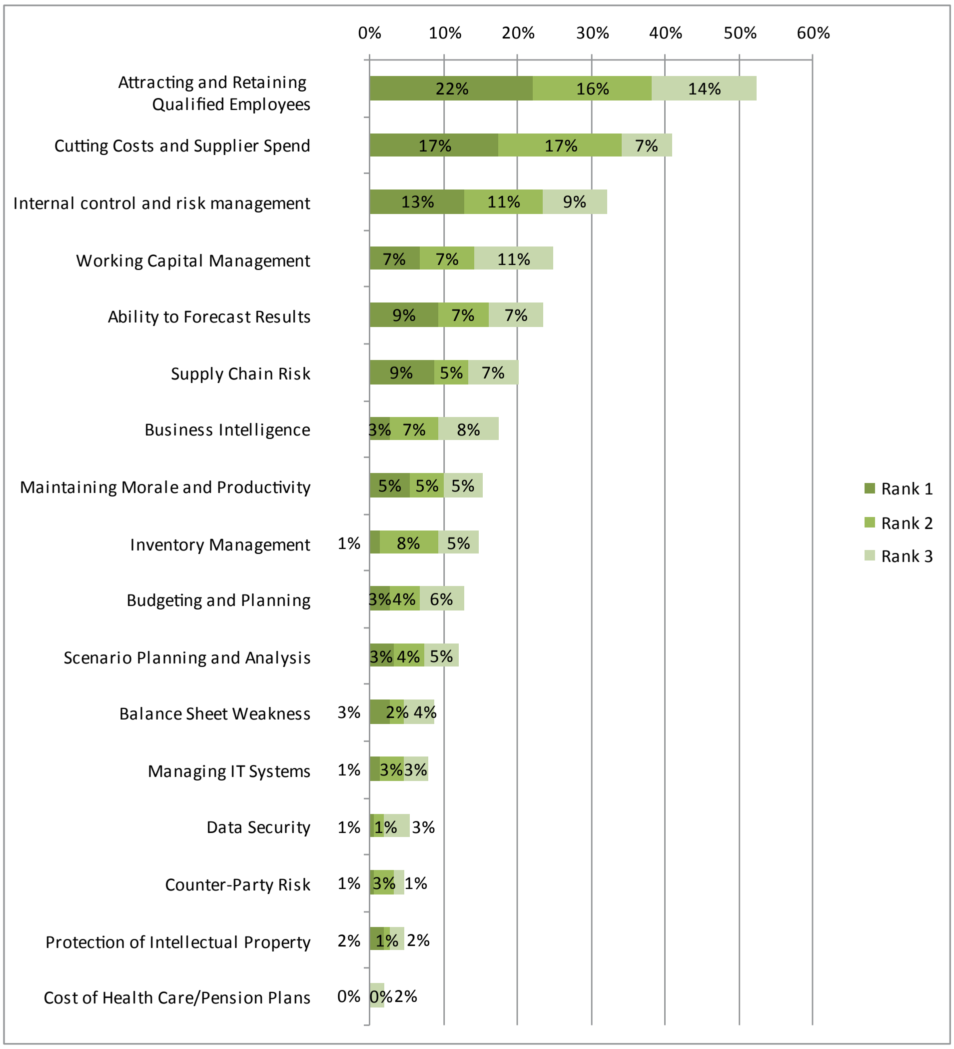
Talent retention remains the top concern

Respondents were also asked to identify and rank the top three internal issues their company faces. As it was in the previous surveys, the top concern remains attracting and retaining qualified employees (22% No. 1 concern; 52% top-three concern). The retention part is presumably the stronger half of this pairing now, given the finding that fewer respondents expect to see intensified hiring.

The second-ranked internal concern is the ability to cut costs and reduce supplier spend, cited by 41% of the executives surveyed (previous quarter: 40%). The ability to conduct internal control and risk management (33%) is the No. 3 internal concern.

Cost cutting was the top internal concern in the last quarter of 2009 and the first quarter of 2010, when Asia was still feeling the after-effects of the global financial crisis. Should cost cutting rise to the top of the list of worries again in future surveys, that may indicate expectations among companies of a double-dip global recession.

Exhibit 8: What are the most serious internal issues that face your company?



Base: 149 respondents. Totals may not add up to 100% due to rounding

Strategic focus: Cost-cutting remains in the mix

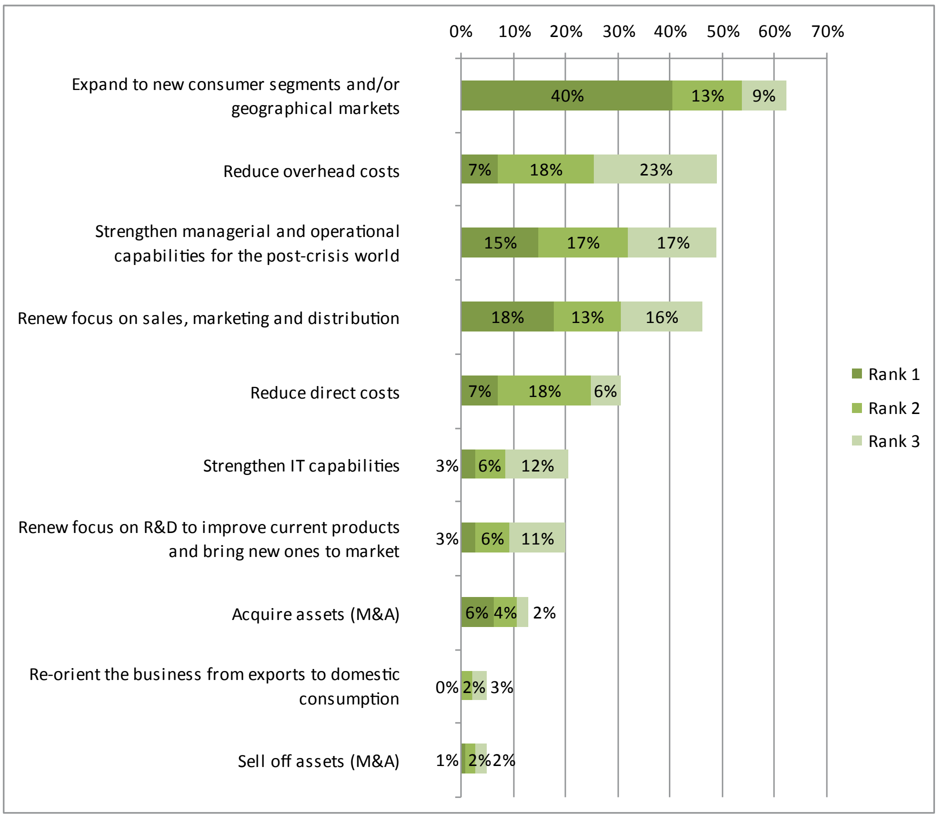
Indeed, there are indications that companies are sharpening the cost-cutting knives again. Cost-cutting receded as a priority last year, but it started to make a comeback in our previous survey, when 45% of respondents identified reducing overhead costs as a top-three strategic focus in the next 12 months. Only 37% regarded cutting overhead as a top focus in the first quarter of 2011.

In the current survey, 48% of respondents now point to reduction of overhead costs as a top-three strategic priority in the next 12 months, with reduction of direct costs identified as a top-three focus by 31% (previous survey: 25%).

That said, the highest ranked priority business areas are still those having to do with expansion and investment. Sixty two percent of the executives surveyed say that their company will remain focused on new consumer segments and/or geographical markets (previous survey: 64%), while 47% will continue to pay close attention to sales, marketing and distribution (down sharply from 61% in the previous survey).

These are also the two areas that are ranked the number one strategic focus by the most number of respondents (40% and 18%, respectively).

Exhibit 9: What is your company's strategic focus in the next 12 months?



Base: 141 respondents. Totals may not add up to 100% due to rounding

About this report

Fieldwork for this online survey was conducted from 3 June to 4 July 2011. Cesar Bacani, CFO Innovation's Editor-in-Chief, devised the questionnaire, analysed the results, and wrote the report.

A total of 165 respondents from Singapore, Malaysia, Hong Kong, Philippines, Indonesia, 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	37%
Malaysia	15%
Hong Kong	9%
Philippines	9%
Indonesia	7%
China	6%
India	4%
Thailand	3%
Vietnam	2%
Australia	1%
Taiwan	1%
Japan	1%
Korea	1%
Other	4%

Total may not add up to 100% due to rounding

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

CFO/Finance Director	45%
Financial Controller	18%
CEO, Chairman, President, Managing Partner or Owner	8%
Finance Manager	6%
Vice President Finance	5%
Other senior finance executive	5%
Other C-level executive or Partner	5%
Treasurer	1%
Other	6%

Total may not add up to 100% due to rounding

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

Fewer than 50	12%
51 to 200	18%
201 to 500	16%
501 to 2,000	17%
2,001 to 5,000	16%
More than 5,000	21%

Total may not add up to 100% due to rounding

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

Less than US$1 million	5%
US$1 million to US$5 million	7%
More than US$5 million to US$10 million	4%
More than US$10 million to US$20 million	7%
More than US$20 million to US$50 million	14%
More than US$50 million to US$100 million	9%
More than US$100 million to US$200 million	9%
More than US$200 million to US$500 million	14%
US$501 million to US$1 billion	11%
Over US$1 billion	20%

Total may not add up to 100% due to rounding

...and engaged in the following industries:

Consulting/Other professional services	14%
Banking/finance/insurance	9%
Industrial equipment	8%
Electronics/software/high-tech	7%
Energy/oil/gas	7%
Food and restaurants	7%
Transportation/travel/hotel	7%
Pharmaceuticals/medical products/ bio tech	6%
Chemicals	5%
Telecommunications	5%
Automotive	4%
Consumer durables, including white goods	4%
Healthcare provider	3%
Retail	3%
Media & entertainment	2%
Metals/mining	2%
Property and construction	1%
Other	9%

Total may not add up to 100% due to rounding

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