Capital Confidence Barometer

Optimism becomes less stable

Economic outlook
Confidence varies by region

Access to capital
Companies taking on leverage

Growth strategies
Organic growth takes a step back

M&A
Growing the top line
Confidence continues in key markets

A majority of CFOs (57%) remain confident in the state of the global economy.

Key findings

57% believe the global economy is improving

87% view credit availability as stable or improving

30% expect to increase their workforce

61% have confidence in corporate earnings

53% are confident in the stability of markets in the short term

44% are confident in the stock market outlook

59% expect the market for M&A deals to improve over the next 12 months
For leading global corporates, striking a balance between risk and reward has rarely been so difficult. Companies are grappling with geopolitical instability, a fragile global economic recovery and seismic shifts in "megatrends" such as structural changes in the workforce and digital transformation — all at a time of unprecedented shareholder activism.

Many executives are now navigating this complexity with parallel priorities. Value is being sought today through a renewed focus on cost-management strategies and returning rewards to increasingly active shareholders.

At the same time, some executives are also seeking value creation and top-line revenue through innovative organic growth and measured dealmaking. Larger, more transformational M&A is on the strategic growth agenda. Pipelines point to only modest increases in deals as low volume becomes the hallmark of a low-growth environment. Increased deal values, rather than volumes, will likely be making headlines in the coming year.

After a prolonged financial crisis and M&A market malaise, companies and boards are opting for quality rather than quantity.

"On a global basis, most CFOs are confident about the economy."

A note from EY leadership

Welcome to the second edition of the CFO Capital Confidence Barometer. Every six months, we survey some 1,600 senior leaders at companies in 54 countries for our Global Capital Confidence Barometer. There are approximately 500 CFOs among them — and this report showcases their most recent views.

The global results show that most CFOs are confident about the economy and many economic indicators. Looking at specific regions, however, we see key differences. North Americans, for example, are especially positive. Buoyed by the economic recovery and more clarity around issues such as US Federal Reserve policies, CFOs there feel optimistic about corporate earnings and credit availability.

In Europe, the Middle East, India and Africa (EMEIA) region in general, more CFOs see their economies improving and are largely confident in bellwethers such as equity valuations and short-term market stability. Scratch the surface, however, and a divergence becomes evident in market outlooks. For example, while CFOs in Western Europe feel positive about recovery, less than half in Eastern Europe and the Middle East/Africa see their economies growing. Nearly one-fifth say conditions are actually worsening.

In Asia-Pacific, most of the region continues to reap the benefits of the economic recovery. China is a top destination for foreign capital. Positivity isn’t limited to China. Nearly 90% of CFOs across Asia-Pacific say their economies are either improving or stable. They report confidence in multiple economic indicators. Nearly 6 in 10 are optimistic about corporate earnings, and 52% are confident in credit availability.

The outlook on financial markets is similarly bullish: 53% are confident in the short-term stability of markets, while 42% have a positive view of equity valuations and the stock market.

We hope you enjoy our latest CFO Capital Confidence Barometer. We are sure you will find useful the insights from your corporate finance counterparts around the world on how they are responding to current conditions.

A note from Pip McCrostie, EY Global Vice Chair, Transaction Advisory Services

For leading global corporates, striking a balance between risk and reward has rarely been so difficult. Companies are grappling with geopolitical instability, a fragile global economic recovery and seismic shifts in "megatrends" such as structural changes in the workforce and digital transformation — all at a time of unprecedented shareholder activism.

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At the same time, some executives are also seeking value creation and top-line revenue through innovative organic growth and measured dealmaking. Larger, more transformational M&A is on the strategic growth agenda. Pipelines point to only modest increases in deals as low volume becomes the hallmark of a low-growth environment. Increased deal values, rather than volumes, will likely be making headlines in the coming year. After a prolonged financial crisis and M&A market malaise, companies and boards are opting for quality rather than quantity.
Economic outlook — confidence varies by region

North America and Western Europe are more optimistic than the rest of the world.

As with real estate, the three most important factors driving a CFO’s optimism concerning the current economic conditions seem to be location, location and location. Marked regional differences exist when it comes to their confidence in the economy. North American CFOs are the most buoyant: two-thirds of them see conditions improving. They are closely followed by their counterparts in Western Europe (61%).

Alternatively, fewer than half the CFOs in Latin America, Eastern Europe and the Middle East/Africa see their economies growing. Those in the Middle East/Africa are the most pessimistic: 18% of them say conditions are worsening.

Similarly, around the globe, confidence in key economic indicators varies widely. For example, there is a 21-percentage point gap between North America-based CFOs and Latin America-based CFOs when it comes to their optimism around credit availability in these respective regions.

Striking differences in regional markets

CFOs in North America and Western Europe are the most optimistic. In a sign that the economic recovery is well underway in their respective regions, roughly two-thirds of them view their economies as moving forward. However, a rising tide is not lifting all boats. In fact, fewer than half of CFOs in three key regions see conditions improving.

Key economic indicators are also erratic

When it comes to corporate earnings, credit availability, the equities markets and overall market stability, CFOs in various regions show widely different levels of confidence. For example, when it comes to short-term market stability, 66% of North American CFOs are optimistic. Contrast this with CFOs in Western Europe (42%) and Eastern Europe (40%), who are far less positive.
Q: What is your perspective on the state of the global economy today?

59% of CFOs in Asia-Pacific say their economy is improving.

Q: Please indicate your level of confidence in the following at the global level:

35% of CFOs in Middle East and Africa are confident about credit availability.
Optimism remains high

Global megatrends converging to shape business and acquisition strategy

Five key global trends are shaping CFOs’ business and acquisition strategy. The so-called “future of work” trend – encompassing the gap in skills between applicants and jobs and competition for talent, among other issues – is having an impact, with 49% of CFOs calling it the most significant trend. Another concern for CFOs is the digital transformation, a catch-all term for changes in technology. In particular, automated processes created by improved technology could be contributing to a shortage of skilled talent.

Political instability, policies are top risks

With geopolitical problems in Ukraine and Syria making news, key economic risks include increased global political instability (29%) and slower growth in emerging markets (28%). The tapering of the US Federal Reserve’s quantitative easing policy remains a top concern for US respondents.
Q: Which of these global trends is most likely to impact your business and acquisitions strategy over the next 12 months?

- **Future of work**: 49% (Business strategy), 38% (Acquisition strategy)
- **Digital transformation**: 40% (Business strategy), 42% (Acquisition strategy)
- **Global rebalancing**: 35% (Business strategy), 30% (Acquisition strategy)
- **Rethinking government**: 31% (Business strategy), 32% (Acquisition strategy)
- **Resourceful planet**: 31% (Business strategy), 35% (Acquisition strategy)

42% of CFOs think the digital transformation will affect their acquisition strategy.

Q: What do you believe to be the greatest economic risk to your business over the next 6 to 12 months?

- **Increased global political instability**: 29%
- **Continued slower growth in key emerging markets**: 28%
- **Inability to effectively manage quantitative easing (tapering)**: 21%
- **Pace of structural reforms in Eurozone**: 12%
- **Inflation**: 6%
- **Deflation**: 4%

29% of CFOs say increased global political instability is their top risk.
Companies taking on leverage

Rising interest rates, combined with unprecedented access to credit, have fueled a shift from cash to debt for financing deals.

A year ago, cash was the primary source of financing for the majority of CFOs (54%). Now nearly half (49%) are relying on debt. The increase in debt financing is likely to increase debt-to-capital ratios. Fully a third of CFOs (34%) put their current debt-to-capital ratio between 25% and 50%, and nearly a quarter (23%) of CFOs plan to increase leverage over the next 12 months.

Global credit confidence at an all-time high

Confidence in the availability of credit has stabilized from six months ago. Nearly 9 in 10 CFOs (87%) believe the market for credit is stable or improving, while only 13% foresee a decline. This development gives companies more options for pursuing strategic growth.

Window for refinancing debt likely closing

With the US Federal Reserve expected to end its policy of quantitative easing, the opportunity to refinance debt may be fading. Still, just 38% of CFOs plan to refinance. The same percentage of respondents said they planned to refinance in October 2013, an indication that the end of quantitative easing has been expected for some time. Companies are instead focused on extending maturities, reducing interest costs and optimizing capital structures as quantitative easing slows.

Excess cash to pay down debt

Debt repayment is the primary use of cash for CFOs looking to return capital to stakeholders – an acknowledgement of its role in the cost of investment. Nearly half (43%) of CFOs plan to pay down debts. Finance executives are also returning capital to stakeholders via dividends (34%) and stock buybacks (23%).
Debt-to-income ratios rise

Q: How do you expect your company’s debt-to-income ratio to change over the next 12 months?

<table>
<thead>
<tr>
<th></th>
<th>April 2014</th>
<th>October 2013</th>
<th>April 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pay down debt</td>
<td>37%</td>
<td>40%</td>
<td>23%</td>
</tr>
<tr>
<td>Paying dividends</td>
<td>34%</td>
<td>47%</td>
<td>19%</td>
</tr>
<tr>
<td>Buy back stock</td>
<td>33%</td>
<td>46%</td>
<td>21%</td>
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</tbody>
</table>

40% of CFOs expect to maintain their debt-to-income ratios

Q: What is your company’s current debt-to-capital ratio?

<table>
<thead>
<tr>
<th>Debt-to-capital ratio</th>
<th>April 2014</th>
<th>October 2013</th>
<th>April 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 25%</td>
<td>40%</td>
<td>40%</td>
<td>45%</td>
</tr>
<tr>
<td>25%-49.9%</td>
<td>34%</td>
<td>32%</td>
<td>30%</td>
</tr>
<tr>
<td>50%-74.9%</td>
<td>17%</td>
<td>18%</td>
<td>17%</td>
</tr>
<tr>
<td>75%-100%</td>
<td>9%</td>
<td>10%</td>
<td>8%</td>
</tr>
</tbody>
</table>

34% of CFOs have debt-to-capital ratio of 25% to 50%

Q: If your company has excess cash to deploy, after organic and inorganic investments, how do you plan to return cash to stakeholders?

- Pay down debt: 43%
- Paying dividends: 34%
- Buy back stock: 23%

43% of CFOs plan to use refinancing to retire maturing debt
Growth strategies — organic growth takes a step back

Fewer CFOs are focused on expansion.

On a global basis, 41% expect to grow in the next 12 months, an 11% decrease from October 2013. At the other end of the spectrum, 18% of CFOs are focused on maintaining stability. This represents an increase of nine percentage points from October 2013.

There are dramatic differences in growth strategies across different regions. For example, half of CFOs in Western Europe are focused on growth, perhaps an indicator that there is nowhere to go but up since the global financial crisis. On the other hand, only 24% of Latin American CFOs are targeting growth, as nations such as Brazil face economic headwinds.

Paradoxically, around the world, more CFOs are moving from low-risk growth strategies to riskier ones. Whereas 40% of CFOs were focused on core products and existing markets last October, just 23% are now concentrated on core products. Most of the decline can be attributed to CFOs prioritizing or changing their mix of products and services offered.

Balanced focus on growth and cost reduction

CFOs are less focused on growth than they were in October 2013, as just 41% say growth is a priority over the next 12 months. Pressure for companies to grow remains, however, and lessons learned from the global financial crisis mean that closer scrutiny on cost structures and operational efficiency is now the norm.

Growth appetite varies across regions

Another sign of the uneven recovery around the world is the differences in growth strategies. But there are some surprises. More CFOs in Middle East/Africa (44%) are focused on growth than their counterparts in North America and Asia-Pacific. Alternatively, CFOs in Latin America are holding the line. They are far more intent on cost reductions and efficiency than growth.

High-risk growth strategies take priority

With fewer companies focused on growth, there is greater opportunity for ambitious companies to differentiate themselves through aggressive strategies. That is likely the reason why R&D spending increased from 7% to 17% since October 2013, suggesting there is greater optimism that innovation can generate growth.
Modest growth expected

Q: Which statement best describes your company’s focus over the next 12 months?

<table>
<thead>
<tr>
<th>Region</th>
<th>April 2014</th>
<th>October 2013</th>
<th>April 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asia-Pacific</td>
<td>5%</td>
<td>18%</td>
<td>39%</td>
</tr>
<tr>
<td>Eastern Europe</td>
<td>15%</td>
<td>50%</td>
<td>35%</td>
</tr>
<tr>
<td>Latin America</td>
<td>4%</td>
<td>25%</td>
<td>47%</td>
</tr>
<tr>
<td>Middle East and Africa</td>
<td>6%</td>
<td>6%</td>
<td>44%</td>
</tr>
<tr>
<td>North America</td>
<td>4%</td>
<td>19%</td>
<td>35%</td>
</tr>
<tr>
<td>Western Europe</td>
<td>3%</td>
<td>16%</td>
<td>31%</td>
</tr>
</tbody>
</table>

18% of CFOs around the world seek to maintain stability

50% of CFOs in Eastern Europe are focused on cost reduction and efficiency

Q: What is the primary focus of your company’s organic growth over the next 12 months?

- Changing mix of existing products and services: 23%
- Increase R&D/product introductions: 17%
- Investing in new geographies/markets: 13%
- Exploiting technology to develop new markets/products: 15%

17% of CFOs are increasing R&D spending
M&A — growing the top line

CFOs see an improving pipeline and are planning for meaningful revenue growth from M&A.

Improving confidence in the global economy and a more positive outlook on the deal market is driving CFOs to be more optimistic about the benefits of M&A. In fact, many CFOs are relying on deals to drive more overall growth. Nearly half (40%) of CFOs are planning for at least 25% of their revenue growth to stem from acquisitions.

While M&A may be seen as a source of growth, interestingly, this may not indicate a marked increase in the number of transactions. In fact, just 28% of CFOs expect their company to pursue acquisitions in the next 12 months, essentially the same amount that said this last October.

Of CFOs that have deals in the pipeline, 69% of them have between one and three deals. This concentrated focus implies that they are applying more and more rigorous, transaction diligence.

Transactions more important to growth

More than one-third of CFOs (36%) predict that acquisitions will provide between 25% and half of their overall revenue growth. Another 4% expect deals to account for more than half of top-line growth.

Deal prospects slip from 2013

Despite the fact that CFOs are counting on significant revenue growth from M&A, fewer of them foresee global deal volume improving. The most recent survey shows that 59% of CFOs expect an uptick in volume, compared to 67% who felt this way in October 2013.
Q: What percentage of your planned growth for the current fiscal year is explicitly assigned to acquisitions?

- Less than 25%: 60%
- 25%–50%: 36%
- Greater than 50%: 4%

April 2014

Q: What is your expectation for global M&A/deal volumes in the next 12 months?

- Improve: 59%
- Remain the same: 35%
- Decline: 6%

April 2014

40% of CFOs expect at least 25% of their growth to come from acquisitions.

59% of CFOs predict that global deal volume will improve.
Focused on a smaller pipeline
CFOs that have deals in the works report that they are concentrating on a select group. More than two-thirds (69%) have between one and three deals in the pipeline, and another 10% are working four deals. This focused approach suggests that CFOs are employing more stringent thoroughness in their transactions.

Aggressive in emerging markets
CFOs are seeking opportunities around the globe. They expect to deploy the majority of their acquisition capital in emerging markets, rather than developed regions. Fully one-third (34%) of their focus is on the BRIC countries, while another 27% is earmarked for non-BRIC emerging markets.

Pursuing quality over quantity
Q: If you have deal(s) in your pipeline, how many for the next 12 months?

- >=5: 21%
- 4: 10%
- 3: 18%
- 2: 34%
- 1: 17%

Q: Where do you expect to deploy the majority of your acquisition capital in the following markets?

- Non-BRIC emerging markets: 27%
- BRIC emerging markets: 34%
- Developed/mature markets: 39%

21% of CFOs report that they have five or more deals in their pipeline.

34% of acquisition capital is targeted for deployment to BRIC emerging markets.
CFOs and their colleagues agree

Q: On which of the following capital management issues is your company placing the greatest attention and resources?

**Raising:** With global credit confidence at an all-time high and expectations rising for future rate increases, there has been an upsurge in the level of capital raising. The number of CFOs focused on raising capital has nearly doubled from the previous survey, rising to 28% from 15%. They are taking advantage of favorable terms to add leverage and refinance now.

- **CFOs**
  - Apr-13: 15%
  - Apr-14: 28%
  - Oct-13: 23%

- **Non-CFOs**
  - Apr-13: 24%
  - Apr-14: 29%
  - Oct-13: 14%

**Preserving:** Maintaining a strong balance sheet and guaranteeing access to liquidity are vital to a rigorous Capital Agenda. But CFOs are continuing to move away from survival mode. Their confidence in global economic conditions is spurring them to be more aggressive.

- **CFOs**
  - Apr-13: 9%
  - Apr-14: 3%
  - Oct-13: 4%

- **Non-CFOs**
  - Apr-13: 9%
  - Apr-14: 3%
  - Oct-13: 5%

**Investing**:
on critical strategies

**Investing:** Despite their confidence in short-term market stability and the environment for equities, the number of CFOs concentrating on investing capital has dropped significantly since the previous survey. CFOs have become more assertive about putting their capital to work.

**Optimizing:** When it comes to adding leverage, refinancing and paying down debt, CFOs have become more active in recent months as they prepare for the impact of the Fed’s tapering policies. Nearly half of CFOs are attending to capital optimization, compared to just 39% who were doing so last October.

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**About this survey**

The Global Capital Confidence Barometer gauges corporate confidence in the economic outlook and identifies boardroom trends and practices in the way companies manage their Capital Agendas – EY’s framework for strategically managing capital.

It is a regular survey of senior executives from large companies around the world, conducted by the Economist Intelligence Unit (EIU). Our panel comprises select global EY clients and contacts and regular EIU contributors.

- In March, we surveyed a panel of more than 1,600 executives in 54 countries; half were CEOs, CFOs and other C-level executives.
- Companies’ annual global revenues ranged from less than US$500m to greater than US$5b: <US$500m (17%); US$500m–US$999.9m (25%); US$1b–US$4.9b (31%); and >US$5b (27%).
- Globally, more than 800 companies would have qualified for the Fortune 1000 based on revenue.
- Company ownership was publicly listed (68%), privately owned (21%), family-owned (6%), government/state-owned (3%) and PE/portfolio-owned (2%).
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