CFO survey: optimism tumbles, employment picture bleak

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Optimism about the U.S. economy has fallen back to recession levels among chief financial officers, who foresee minimal increases in hiring, weak consumer demand and heightened economic uncertainty, finds a Duke/CFO Magazine survey.

Optimism about the U.S. economy has fallen back to recession levels among chief financial officers (CFOs), who foresee minimal increases in expected hiring, weak consumer demand and heightened economic uncertainty.

Credit is still tight for small firms and many firms continue to hoard cash. Without improvement in the economy, CFOs say earnings growth and capital spending will falter within six to 12 months.

These are some of the findings of the most recent Duke University/CFO Magazine Global Business Outlook Survey. The survey, which concluded Sept. 10, asked 937 CFOs from a broad range of global public and private companies about their expectations for the economy. (See end of release for survey methodology.) The research has been conducted for 58 consecutive quarters. Presented results are for U.S. firms unless otherwise noted.

SUMMARY OF FINDINGS

-- CFO optimism about the U.S. economy has fallen to 49 on a zeroto-100 scale, well below the rating of 58 from the last quarter. Pessimists outnumber optimists four-to-one. European CFOs' optimism rate is 58; Asian CFOs' rate is 70.

-- Half of CFOs say they will cling tightly to cash due to economic uncertainty and as a liquidity buffer. The other half will spend some cash reserves in the next year, primarily for investment, to pay down debt and to make acquisitions.

-- Earnings are expected to rise 12 percent and capital spending almost 7 percent in the next 12 months. However, nearly half of CFOs say unless the overall economy improves, there is only a six-month window during which they can maintain this level of growth.

-- U.S. CFOs expect to increase domestic full-time employment by 0.7 percent in the next year. Nearly one-fourth of all recent hires have been contract and temporary employees.

-- Credit markets remain tight, especially for small companies. Most CFOs believe financial reform will add costs and restrictions that will dampen lending.

-- CFOs' economy-wide concerns include federal government policies, weak consumer demand, price pressure and the weak national employment outlook. By a wide margin, the top concern among CFOs about their own businesses is the struggle to maintain profit margins, followed by rising health care costs and low employee morale.

-- Exports are expected to increase by 50 percent over the next five years.

OPTIMISM PLUNGES

Optimism about the overall economy fell at 53 percent of U.S. firms and increased at only 14 percent. The optimism rate of 49 is at a level not seen since the first quarter of 2009, when CFOs rated the economy at 40.

"The CFO optimism index has proven to be an accurate predictor of future economic performance," said Julia Homer, executive vice president for content at CFO Publishing LLC. "Therefore, this dramatic drop in optimism bodes poorly for the economic outlook. Half of CFOs say there is only a six-month window -- and another one-fourth believe it's a 12-month window -- during which they can maintain current levels of business activity without improvement in the overall economy."

EMPLOYMENT STAGNANT

U.S. companies expect full-time domestic employment to inch up by 0.7 percent over the next year, while temporary employment will increase 0.8 percent. The labor picture is about the same in Europe, but much stronger in Asia (with expected growth of more than 5 percent).

"This rate of U.S. employment growth will increase payrolls, but not put a dent in the unemployment rate due to growth in labor force participation," Homer said. "Another negative employment trend is the recent surge in hiring contract and temporary employees rather than permanent workers."

U.S. CFOs say nearly one-fourth of recent hiring has been targeted at contract and part-time employees, up from 17 percent prior to the recession.

CREDIT CONDITIONS

Compared to a year ago, 30 percent of companies say borrowing has become more difficult, compared to 25 percent who say borrowing is easier.

"There has been no progress in fixing the credit problem over the last year," said Campbell R. Harvey, a professor of finance at Duke's Fuqua School of Business and founding director of the survey. "Indeed, half of the small businesses say credit conditions are worse than in 2009.

"The math is simple. A) Banks are sitting on cash because of their poor health and general uncertainty. B) Small and medium-sized firms have employment-generating projects that they cannot get financed because banks will not extend credit. C) In usual circumstances, small and medium-sized businesses account for the majority of employment growth. A+B+C implies we are stuck at 9 or 10 percent unemployment," Harvey said.

Harvey added that "recent regulatory reform has not helped. Only 5 percent of CFOs consider the Dodd-Frank legislation as a positive -- and that number excludes all firms in the finance industry. The main concerns about the recent reform are that it will lead to increased compliance costs and make borrowing more difficult. CFOs also expect higher banking fees. Some of these increased costs and fees will be passed on to customers, and others will hurt the bottom line."

WHEN WILL CASH BE UNLEASHED?

"Cash exists in two locations: bank reserves and balance sheets of healthy companies," Harvey said. "Banks show no sign of unfreezing credit. They are lending to the government, not to businesses. However, U.S. firms are sitting on over $1.8 trillion in cash. When will it be unleashed?"

The survey results show 50 percent of respondents have no intention of deploying their cash over the next 12 months. More than half of responders say they will continue to sit on cash for liquidity to protect against another round of credit tightening and general economic uncertainty. Of the 50 percent that will deploy cash, only 56 percent will allocate to capital spending and investment.

"We were especially interested in the type of capital spending that creates jobs," Harvey said. "The survey shows only 22 percent of firms say their new capital spending will lead to hiring. This bodes very poorly for employment in 2011."

EXPORTS, EARNINGS, CAPITAL SPENDING: GOOD NEWS?

Export volume is expected to increase by about 50 percent over the next five years. Exports constitute about 9 percent of current sales by U.S. companies and are expected to grow to a 11 percent share of 2015 sales. This increase in export share accounts for about half of the growth in the dollar value of exports; the other half of export growth will occur as the overall economy grows.

"President Obama has stated a goal of doubling exports over the next five years," said John Graham, a professor of finance at Fuqua and director of the survey. "CFOs indicate export growth will achieve only about half of this goal. On top of this, some of the growth in U.S. exports will be offset by decreased domestic purchases by U.S. firms as imports continue to rise. Based on these numbers, the net boost to GDP growth from increased exports is likely to be small, no more than 0.5 percent per year."

Earnings are expected to rise 12 percent and capital spending 7 percent, both up from last year, but down from last quarter. As a warning, however, three-fourths of CFOs indicate they will not be able to maintain this level of earnings and capital spending growth beyond the current year unless the overall economy improves.

TOP CONCERNS

Top concerns for U.S. CFOs include the federal government's agenda and weak consumer demand. U.S. CFOs, who expect to raise the prices of their products by 1.4 percent, are also worried about price pressure from intense competition.

For the second quarter in a row, maintaining employee morale is among the top company-specific concerns. Health care costs also have reappeared among the top worries, as CFOs expect corporate health care payments to rise 10 percent in the next year.

ASIAN RESULTS

Due to wage increases among manufacturing employees, more than one-third of Asian CFOs expect manufacturing sector growth to fall by a moderate or large amount.

Nearly half of Asian CFOs believe stricter enforcement of their country's immigration policies would have a negative effect on the economic growth of their country. In comparison, 35 percent of U.S. firms feel this way.

Top concerns focus on intense price pressure, global financial market instability, weak consumer demand and concern about government policies.

Attracting and retaining qualified employees is a major concern for Asian companies, especially in China. Other top company-specific concerns include achieving profit margins and maintaining employee morale and productivity.

Asian CFOs expect capital spending to increase by about 9 percent, and say earnings will climb by more than 13 percent.

About 70 percent of Asian companies expect to unleash cash reserves over the next year. Among these firms, primary uses of the cash include capital spending, research and development, and increasing employee pay and benefits.

EUROPEAN RESULTS

The employment picture in Europe remains sluggish. In the next 12 months, European CFOs expect to increase domestic full-time employment by 0.5 percent. Twenty-six percent of European hiring during the past year has been of contract and part-time employees.

Earnings will increase about 11 percent, while capital spending will rise 3 percent.

Only 42 percent of European firms say they will unleash cash reserves in the next year. Many say they continue to accumulate cash as a liquidity reserve.

More information: This is the 58th consecutive quarter the *Duke University/CFOMagazine Global Business Outlook* survey has been conducted. The survey concluded Sept. 10 and generated responses from 937 CFOs, including 569 from the U.S., 135 from Europe, 130 from Asia (not including China), and 103 from China. The survey of European CFOs was conducted jointly with Tilburg University in the Netherlands. Results in this release are for U.S. companies, unless otherwise noted.

Provided by Duke University