

CFOs indicate they would be willing to accept a solution to the 'fiscal cliff' that includes tax increases, survey finds

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Chief financial officers say going over the "fiscal cliff" will lead to dramatic slowdowns in hiring and business spending in 2013 and will continue to hurt firms for years to come.

CFOs also don't see the solution as solely cutting [government spending](#). Instead, a large majority prefer a plan like Simpson-Bowles, which pairs two dollars of spending cuts with each dollar of tax increases.

These are among the findings in the latest Duke University/CFO Magazine [Global Business](#) Outlook quarterly survey of more than 900 CFOs, which concluded Dec. 7.

"It is shocking that CFOs overwhelmingly support Simpson-Bowles, which includes tax rate hikes to raise revenues," said John Graham, a professor of finance at Duke's Fuqua School of Business and director of the survey. "CFOs generally prefer less taxation across the board, so their willingness to accept tax increases is dramatic."

CFOs are very concerned about the possibility of the U.S. not finding a solution to the budget impasse. More than 70 percent say they will reduce hiring if no solution is reached and the U.S. goes over the fiscal cliff. Another two-thirds indicate they will cut business spending.

"The survey offers strong evidence that capital spending will be slashed

under a 'cliff' scenario," said Campbell Harvey, a Fuqua finance professor and founding director of the survey. "CFOs would also cut spending and hiring under a 'kick the can down the road' scenario. Capital spending would be robust only under an approach like Simpson-Bowles."

CFOs indicate the damage brought on by the fiscal cliff would be long-lasting. More than two-thirds say their firms will be worse off five years from now if Congress and President Obama can't reach a deal by Jan. 1 to avoid a dramatic combination of spending cuts and tax increases. Fewer than 5 percent of U.S. CEOs think that going over the fiscal cliff is a desirable way to address the [budget deficit](#).

The Global Business Outlook survey has been conducted for 67 consecutive quarters, and spans the U.S., Asia, Europe and Latin America, making it the world's longest running and most comprehensive research on senior finance executives. Presented results are for U.S. firms unless otherwise noted.

Additional significant findings

- Given the possibility that the U.S. will go over the fiscal cliff, CFOs expect no net hiring and only 2.5 percent growth in capital spending. The size of bonuses will shrink at about 40 percent of firms and increase at only 20 percent compared to last year.
- The U.S. CFO Optimism Index dropped in the third quarter. In Europe, optimism increased. Latin American optimism is much stronger, as is optimism in Asia (with the exception of Japan).

Increased pessimism and top concerns

The fiscal cliff is among the greatest concerns affecting the corporate

sector, trailing only weak consumer demand among external concerns. Worries about governmental policies, intense price pressure and the federal budget deficit round out top external concerns of CFOs.

The difficulty in maintaining profit margins is the top concern of internal U.S. firms. Other worries include the cost of health care, attracting and retaining skilled workers, and employee morale.

"These concerns have led to a continued erosion of optimism about the U.S. economy," said Kate O'Sullivan, editorial director at CFO Magazine. "Optimism has fallen to 51 out of 100, down from 60 last spring, and even slightly below Europe.

This is worrisome because historically reduced optimism foretells slower economic activity over the next year."

Optimism is flat but reasonably strong in Asia (62) but weak in Japan (49). Optimism is increasing and strong in Latin America (66).

Watch Professor John Graham talk about the results:

Hiring, spending, earnings, dividends

Corporate plans are flat for domestic hiring, with only a meager 0.1 percent increase expected in the U.S. This implies a rising unemployment rate in 2013.

CFOs plan to increase capital spending by just 2.5 percent over the coming 12 months, down from 7.3 percent in the spring. This is the fourth consecutive quarter spending plans have declined.

Dividends will soar by 12 percent over the next 12 months, in part because of the surge in year-end 2012 dividends due to the likelihood of

tax hikes in 2013.

Employee benefits, training and bonuses

Eighty-three percent of U.S. CFOs say their firms will pay bonuses this year. Among these firms, however, nearly 40 percent say the bonus will be smaller than last year, with 21 percent saying substantially smaller. Another 40 percent of firms say bonuses will be about the same size as last year.

Many U.S. firms reduced payments toward employee benefits and training during the recession. Few of these companies expect the company contribution toward these expenses to increase back up to pre-recession levels anytime soon.

Eighty-four percent of companies say that in 2013 their contribution toward health care benefits will remain below pre-recession levels. Seventy-four percent of firms say their contributions toward retirement benefits will remain depressed.

Fifty-eight percent say 401(k) contributions are still below pre-recession levels. And 57 percent of companies still have not restored employee training to pre-recession levels.

Finally, employees at 41 percent of firms will continue to work fewer hours next year, compared to pre-recession levels. European firms also indicate a slow rebound in restoring employee-related spending, though the rate of restoration is greater than in the United States.

Additional Latin American results

Latin American CFOs' optimism jumped to 66 out of 100, up from 60

last quarter. This is good news for U.S. multinationals, as 41 percent of U.S. CFOs say that slowing Latin American growth, should it occur, would harm their firms.

About half of firms in Spanish-speaking Latin American countries say that slower Brazilian growth would hurt their companies in 2013, and 70 percent of Brazilian CFOs say that slower growth in the rest of Latin America would hurt their companies.

Among Latin American companies that plan to pay bonuses, only one-fourth of these companies saying the bonuses will be bigger than last year.

In contrast to the U.S. and Europe, only about one-fourth of Latin American companies reduced employee-related benefits during the past five years, and among those that did, about two-thirds say in 2013 employee-related spending will be equal to or exceed pre-recession levels. Training is especially important in Latin America, where 84 percent of companies increased spending in recent years.

Revenues should grow rapidly in 2013 (13 percent), as should capital spending (12 percent) and earnings (11 percent), say Latin American CFOs. Inflation and wages will also rise by nearly 7 percent, however.

The difficulty in maintaining profit margins is the top internal concern for Latin American companies. Other worries include difficulty attracting and retaining skilled workers and maintaining employee morale.

Additional Asian results

Optimism among Asian CFOs (excluding Japan) is 62 out of 100. Japanese CFOs are much less optimistic than their peers, rating their

optimism at 49.

Eighty-six percent of Asian companies plan to pay bonuses, but these will be smaller at 45 percent of firms.

Employment will increase by about 2 percent on average in China, 0.2 percent in Japan and by 5 percent in the rest of Asia, say CFOs in the region. Wages are expected to rise by about 7 percent in Asia, except in Japan, where wages will remain flat.

Top external worries among Asian CFOs include global economic instability and intense price pressure. Top internal concerns include maintaining profit margins, difficulty attracting and retaining skilled workers and employee morale.

Territorial disputes with China have adversely affected the business prospects of many Japanese firms. Three-fourths of Japanese companies say their capital spending plans have declined due to the Chinese dispute (22 percent say the decrease is moderate or worse), and half say that hiring plans have been negatively affected. Chinese companies have also been affected, although not as severely, with 45 percent saying the dispute has led to curtailed spending plans. Only 15 percent say the dispute has affected hiring.

Nearly 90 percent of CFOs in Japan say restrictions on the use of electricity (due to natural disasters and their impact on nuclear power production) have affected their companies. Nearly 40 percent say these negative effects have been moderate or worse.

Additional European results

The economic outlook in Europe may have bottomed out. European optimism remains low, but has rebounded to 52 (out of 100), compared

to 49 last quarter.

Layoffs will continue in Europe, with full-time employment expected to shrink by 1 percent (an improvement from a negative 2.6 percent employment outlook last quarter). [Capital spending](#) is expected to increase 3 percent, up sharply from a 5 percent decrease last quarter. Earnings growth will be negligible.

Top concerns for European CFOs include weak demand, intense pressure on profit margins, economy-wide financial instability, attracting qualified workers and liquidity concerns.

European firms are slow to reinstitute cuts made during the recent recession. Sixty-five percent of firms say their contributions toward retirement benefits will remain depressed. Fifty-eight percent of companies still have not restored employee training to pre-recession levels. Finally, workers at 42 percent of firms will continue to work fewer hours next year, compared to pre-recession levels.

Nearly 70 percent of European companies plan to pay bonuses, but these will be smaller than they were last year at 61 percent of [firms](#).

More information: www.cfosurvey.org/

Provided by Duke University

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