Growth expectations improving

The Deloitte/SEB CFO Survey

Spring 2014 results

Contents

Welcome to the latest edition of the Deloitte/SEB CFO Survey!

We are excited to present the spring 2014 results of the Deloitte/SEB CFO Survey and hope you find our accompanying analysis both stimulating and valuable. Please send us all feedback together with any suggestions for improvement to help us ensure the Deloitte/SEB CFO Survey remains an essential resource for your daily work.

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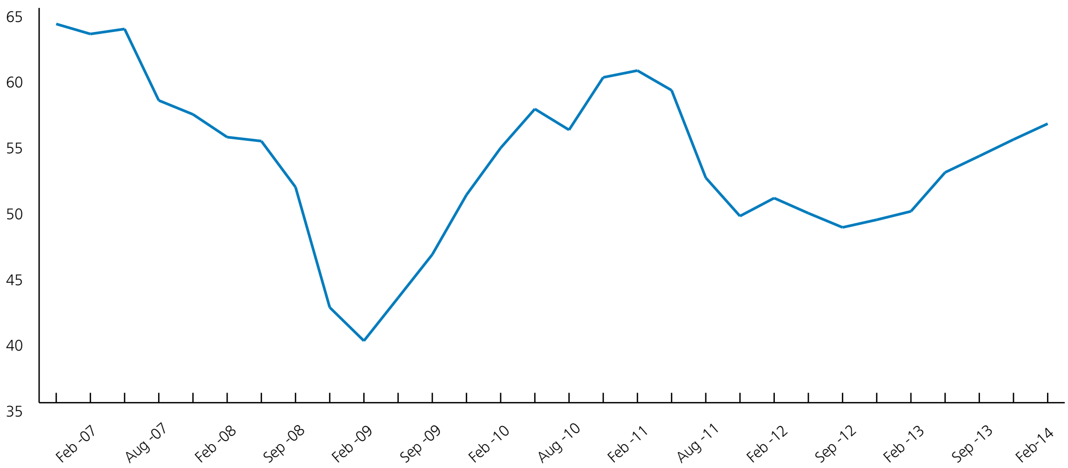
Lower unemployment as growth exceeds trend in 2014

Swedish GDP accelerated in the final quarter last year confirming the upturn signalled by forward looking indicators. The Deloitte/SEB indicator increased to 56.2 in February 2014, its highest level since May 2011. However, despite improvements in the domestic economy, for example in terms of employment and consumer confidence, export performance remains sluggish. SEB forecasts GDP growth of 2.7 per cent in 2014 and 3.2 per cent in 2015.

Swedish CFO Index



The Swedish CFO index for February 2014 is 56.2, which reflects positive expectations. The index is based on four components; business climate, financial position, willingness to lend and counterparty default risk. The four component indices increased in February 2014 to 50.8, 58.5, 66.7 and 48.9, respectively.

Mixed signals from manufacturing

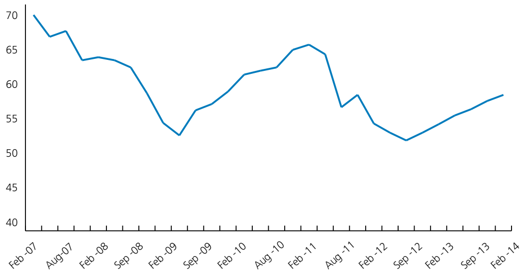
Despite rising sentiment indicators since the first half of 2013, industrial production and merchandise exports have remained weak. This may be due to the unusual combination of a strong krona and poor global demand, making it difficult for manufacturers to keep pace with international expansion. However, surveys from the NIER and Statistics Sweden show that manufacturing capacity utilisation has increased. Also, the Deloitte/SEB indicator has continued to trend higher. Further, manufacturers plan relatively expansionary capital spending this year. We believe special circumstances explain why official export and production figures for the second half of 2013 exaggerate the underlying weakness, a view supported by the slight improvement in exports reported at the beginning of this year. SEB expects total exports to increase by 3.5 per cent in 2014 and 6 per cent in 2015.

With demand picking up, capital spending is very likely to begin rising again, an assessment corroborated by the latest Statistics Sweden survey. There are also many indications that the upturn in residential construction will continue this year. Residential investments are expected to increase by around 20 per cent both in 2014 and 2015, contributing approximately half a percentage point annually to total GDP growth. At the same time, it is difficult to see how a substantial rise in new construction of owner-occupied housing can be consistent with the Riksbank's aim to prevent increases in household debt. Overall the Deloitte/SEB CFO survey comes to the same conclusion; business conditions are regarded as either average or favourable; more companies plan to raise investments (three times more intend to increase than decrease spending); and almost 50 per cent of firms expect to boost capacity utilisation.

Financial position improves

The survey continues to show that companies regard their financial positions and banks' willingness to lend as positive. As before, the two sub-indices have the highest readings of the index's four components. In particular, the Financial Conditions Index increased to 58.5 in February from 56.4 last September, while the Lending Willingness Index rose to 66.7 from 63.1. Some 90 per cent of companies see lending attitudes as either favourable or very favourable which, together with improvements in cash flow, supports higher investments. At the same time however, firms also say they prefer to use surplus cash to pay down debt or invest strategically overseas.

Financial position



Consumption drives growth

There are relatively clear signals that consumption is set to accelerate. Consumer confidence has trended upward since mid-2013 and is now above its historical average, despite a setback at the beginning of this year. An increasingly strong labour market, together with rapidly rising wealth and incomes, suggests that the upturn will continue this year. Retail sales of cyclically sensitive durable goods, in particular, are now growing faster than at any time since 2011. Tax cuts equivalent to nearly 1 per cent of income and rising real wages are producing relatively large increases in income. SEB forecasts that consumption will rise by 3 per cent both in 2014 and 2015, while the current historically very high household savings ratio will decrease slightly. The risk of weaker consumption growth remains linked to a fall in house prices. Although the downturn in prices in Norway has increased uncertainty, SEB expects Swedish house prices to increase by around five per cent this year before stabilising in 2015.

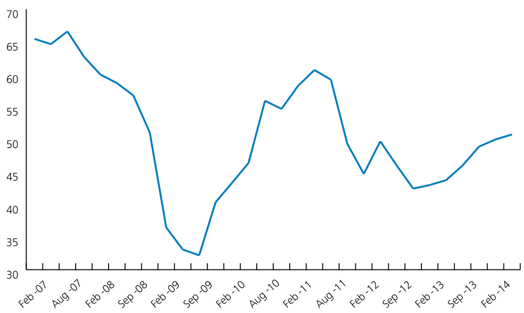
Unemployment declines

Job creation has continued to exceed expectations, though sharply rising labour supply has helped prevented falls in unemployment. Labour supply is being driven both by strong population growth and rising labour force participation. However, there are many signs that unemployment will begin to fall early this year, due to a combination of stronger job growth and slower expansion in the labour force. According to the NIER's Business Tendency Survey, hiring plans have become increasingly bullish over the past 5-6 months. Due to rapid population growth, labour supply looks set to continue rising rapidly. SEB expects unemployment to fall to 7.6 per cent at the end of 2014 and to 6.8 per cent at the end of 2015. Risks of increased wage pressure over the next couple of years are small. Significantly, even the lowest unemployment rate in the past 20 years (around 5.7 per cent) had no significant effect on inflation.

Inflation well below target

Price pressures have remained very low, with CPIF inflation (CPI excluding interest rates) below 1 per cent and CPI close to zero. Further, the combination of historically small collective pay agreements for the next 2-3 years and weak international price pressure indicates continued low inflation in 2014-2015. While decreasing downward pressure from previous krona appreciation and slightly higher pay rises suggest inflation will increase slightly during the second half of 2014, SEB expects CPIF to remain well below the Riksbank's target throughout our forecast period. It also forecasts that CPI inflation will rise above 2 per cent during 2015, as expected Riksbank key interest rate hikes inflate mortgage interest costs. The main risk of higher inflation is that a stronger global economy will result in higher prices for energy and other commodities. With wages and salaries likely to increase at rates well below the historical average for the next couple of years, and with trends clearly exerting downward pressure on many commodities a key factor for CPI, downside inflation risks dominate both in 2014 and 2015.

Business conditions



Inflation target regains lost ground

Stronger economic growth and falling unemployment suggest that December's key interest rate cut was the last in this cycle, although we still see a 35 per cent probability of a further reduction. We assume that continued low inflation and poor resource utilisation will delay key rate hikes until spring 2015 and that the Riksbank will hike twice, bringing the repo rate up to 1.25 per cent at the end of 2015.

The minutes of the central bank's last monetary policy meeting (December 2013) indicate a paradigm shift, with long-term low inflation becoming the centre of attention at the expense of financial stability. We expect low inflation to remain in focus. This implies that the central bank will continue to signal a downside risk to its repo rate forecast during most of this year. It is also likely that one or more board members will argue in favour of more interest rate cuts and eventually dissent from a decision to leave the key rate unchanged.

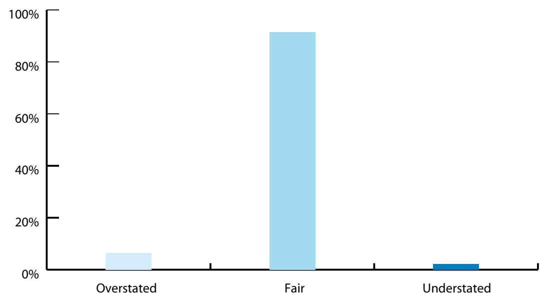
Krona continues to appreciate

The krona has strengthened by around 3 per cent in trade-weighted terms since the Riksbank cut its key rate on December 17. With the EUR/SEK exchange rate appreciating rapidly from 9.10 to 8.80, there is a risk that Swedish inflation will prove lower than estimated in coming months, provoking expectations of further rate cuts and causing foreign investors to sell SEK. However, as SEB's main scenario is that CPIF will bottom out and the Riksbank will leave its key rate unchanged, it expects the krona to benefit from relatively strong economic conditions. In addition, increasing expectations about new ECB measures will exert general downward pressure on the euro against most other currencies. The krona should benefit from rising global growth. We therefore reiterate our forecast EUR/SEK rate of 8.50 at the end of 2014, and raise our estimate slightly to 8.40 at the end of next year. We project a USD/SEK rate of 6.64 at the end of this year and 6.72 at the end of 2015.

Hot topic – Impact of emerging market concerns

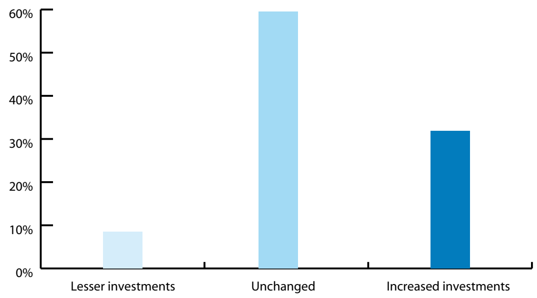
While most CFOs fully share current market concerns over developments in emerging markets, they still plan to raise investments and expect capacity utilisation to improve over the next six months. Although the increase will occur from an abnormally low level, it nevertheless indicates greater self-confidence and better prospects going forward.

Do you think financial market concerns relating to emerging markets are:



A very high proportion of CFOs surveyed say they regard emerging market concerns as justified. For some time, unease has resulted in low investments. The current Russian-Ukrainian crisis, countries to which several Swedish companies are significantly exposed, further illustrates the serious and less easily foreseen risks involved. In view of current concerns over developments in emerging markets, we asked CFOs for their views on investments and production capacity over the next 12 months.

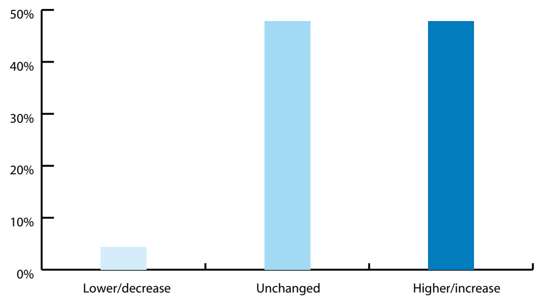
How will your company's investment plans with respect to plants and personnel change during the coming 12 months?



Approximately 60 per cent of CFOs questioned replied that they expect no change in their company's investment plans for plant and personnel over the next 12 months, while around 30 per cent believe they will increase spending. This is interesting, given the large production deficit in recent years. More investments in plant and personnel imply greater production and higher output going forward, as well as a higher inflation rate and increased interest rates.

How will your company change its capacity utilisation and production plans during the coming 12 months?

The CFOs surveyed answer this question consistently with their replies to the last. They emphasise that companies are preparing to raise output, not at some indefinite point in the future but within the next 12 months. This is clearly a positive development, suggesting increased momentum and a further improvement in market sentiment.

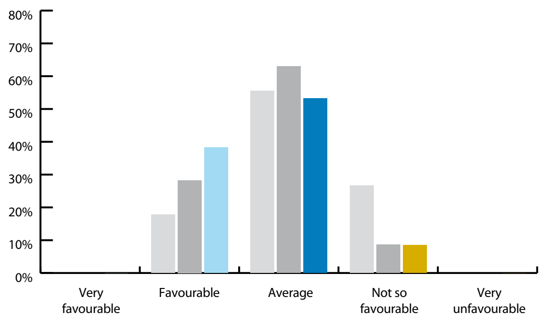


Business conditions and outlook

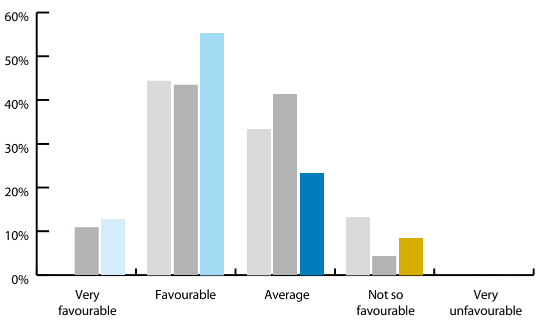
Overall, CFOs are increasingly positive towards current and prospective business conditions. Most companies are generally optimistic on the prospects for the rest of this year. Respondents regard their financial positions as favourable, while most expect to improve their operating cash flows.

1. Business conditions for your company in the next 6 months are seen as:

Since our last update in September, business conditions have continued to improve, according to CFOs surveyed. Today, approximately 40 per cent of CFOs (an increase of 10 percentage points compared to last September) regard business conditions during the next six months as "favourable". Probably, the increase is attributable to a more positive attitude among those who regarded them as only "average" last fall. This development may correlate very closely with surprisingly positive Q4 GDP data reported in February.

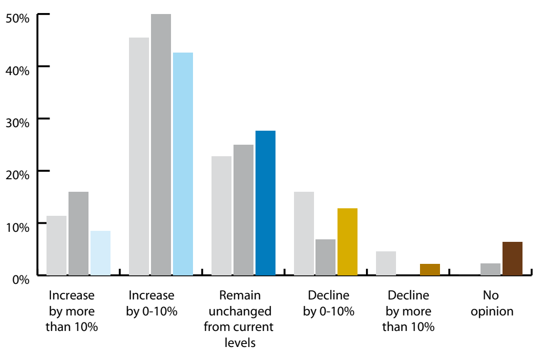


2. The overall financial position of your company is seen as:



The overall financial position of companies has improved, with just over 55 per cent (an increase of 10 percentage points since last September) of CFOs surveyed regarding their position as "favourable". While a limited number of CFOs (amounting to only a few per cent) believe the financial position of their company has worsened, on average companies now see a brighter financial future than last September. This view may reflect the general stabilisation of the European financial environment, as well as persistently low interest rates. CFOs surveyed have expressed increasing concern over interest rates going forward. Altogether, we conclude that companies are financially sound and the outlook increasingly positive. This is a key finding of our survey.

3. How do you expect operating cash flow in your company to change over the next 12 months?



Swedish CFOs retain positive cash flow expectations for the next 12 months, although they are not as wholly optimistic as they were in our survey last fall. Today, some 51 per cent of respondents expect cash flow to increase, signaling a still very positive outlook. However, following higher operating cash flows in recent quarters, it is hardly surprising companies forecast a more stable development going forward. A total of 15 per cent of CFOs believe operating cash flows will decline, which is surprisingly high given the current overall positive outlook.

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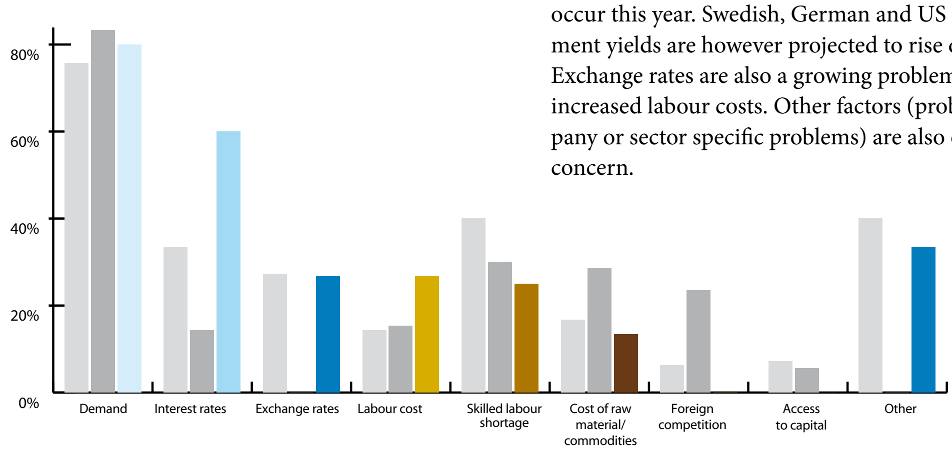
Prospects and concerns

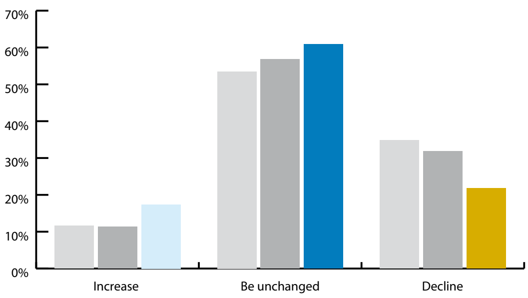
As in our previous surveys, demand remains the greatest concern for Swedish CFOs. However, they are becoming more worried about the threat of rising interest rates following the recent prolonged period during which they have remained low. Respondents are increasingly concerned about the cost and availability of skilled labour, a development that usually signals improving market conditions. Positively, CFOs are more confident of increased employment in Sweden and abroad.

4. What are the greatest concerns for your company in 2014?

As in previous surveys, demand is the greatest concern for CFOs. However, we see increasing worries over interest rates, suggesting that higher interest rates are of real concern. Given the low interest rate environment over the past few years, CFOs may think rates may slowly return to pre-crisis levels, although this view is inconsistent with near-term consensus central bank rate forecasts. It is certainly unlikely to occur this year. Swedish, German and US government yields are however projected to rise during 2014. Exchange rates are also a growing problem, as are increased labour costs. Other factors (probably company or sector specific problems) are also of growing concern.

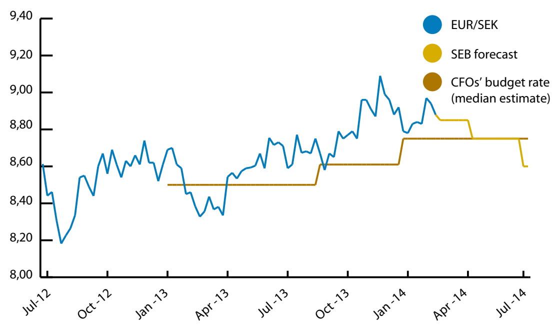


5. The number of employees in your company in Sweden is, in the next 6 months, expected to:



The percentage of CFOs believing their workforce in Sweden will remain unchanged over the next six months has increased slightly to just over 60 per cent, while the share of respondents that think they will fall has declined by approximately 10 percentage points. Probably, the change reflects a larger proportion of CFOs that expect the workforce to increase, a view endorsed by 20 per cent of respondents. Nearly 40 per cent also stated they expected employment abroad to increase.

6. What is your EUR/SEK budget rate for the financial year 2014?



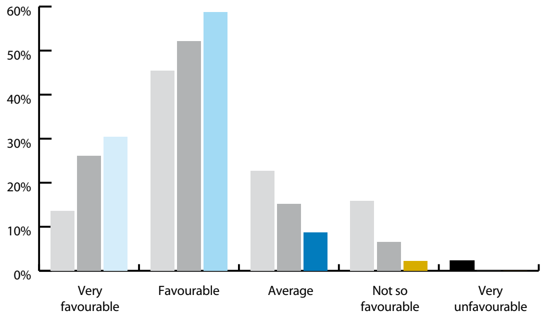
The median EUR/SEK budget rate is 8.7, representing the average (or median) of the SEB 2014 forecast. This is significant as CFOs polled in previous surveys have tended to overestimate the actual EUR/SEK rate, and the speed at which the krona has appreciated. This probably caused several companies to suffer in previous periods. Now, CFOs have apparently prepared their budgets based on the forecast, which implies that they are seeking to minimise the possibility of incurring currency related losses.

Financing

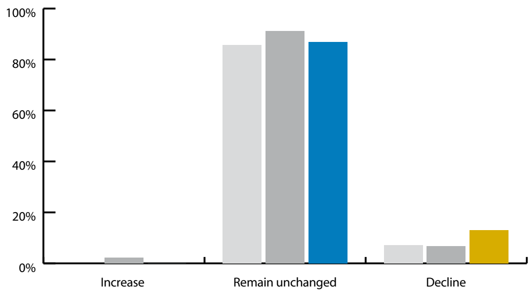
The attitude of financial institutions to lending has continued to improve since our survey last September to stand at new record highs, strongly signaling increased confidence and financial stability. Currently, such institutions appear more focused on growth, than on balancing restrictions and new regulations on lending.

7. The lending attitude of financial institutions toward your company is seen as:

Also the perceived lending attitude towards companies surveyed has improved. Almost 90 per cent of CFOs regard the lending attitude of financial institutions toward their company as “favourable” or “very favourable”, compared with around 75 per cent last September. Probably, this also reflects the fact that interest rates are lower now than in September.

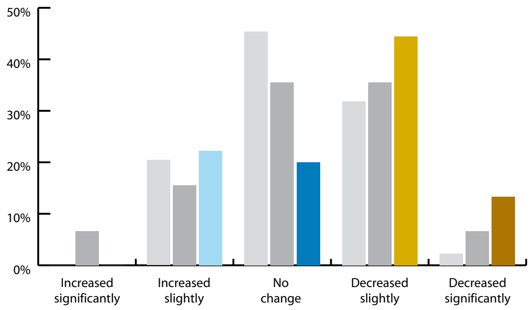


8. The probability for counterparties’ default in the next 6 months is expected to:



In our last survey, there was little difference between present and historical values. Also currently, the perceived probability of counterparties defaulting in the next six months is thought slightly positive. Some 13 per cent of CFOs surveyed believe default will become less likely, with 87 per cent saying the risk will remain unchanged. We regard the overall positive sentiment shown by the survey as a sign of stability and recovery, with almost no outright concerns expressed regarding defaults by counterparties.

9. How has the level of financial risk on your balance sheet changed over the last 12 months?



Most CFOs believe financial risk on their balance sheets has continued to decrease over the last 12 months. Respondents report an ongoing improvement in conditions affecting their exposure to financial risk. Overall, sentiment has become increasingly positive since our fall survey. Most companies are seen as financially stable, while market conditions have generally improved.

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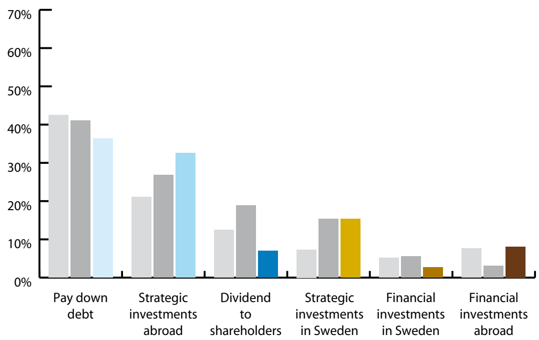
Strategic opportunities

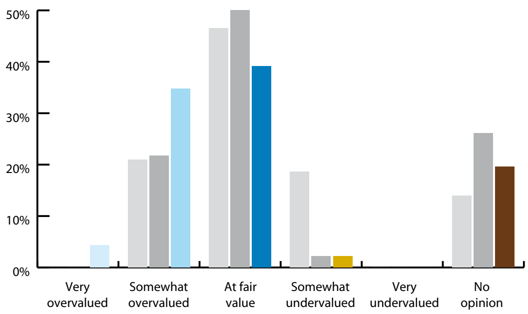
Responses received confirm expectations of increased M&A activity. We see a further recovery in such transactions over the next 12 months, with several large deals occurring at the start of this year. CFOs with current cash surpluses still prefer to make strategic investments and to pay down debt, confirming a slightly more positive view of future prospects.

10. Assuming a current cash surplus position, how would you prefer to use the money in the next 6 months?

Changes since last September are less dramatic than those that have occurred since last spring. During the Q4 reporting season, companies were more interested in paying dividends to shareholders, as forecast in our last survey. Now, following the announcement of generous 2013 dividends, firms have refocused elsewhere, preferring instead to pay down debt, with nearly 40 per cent of CFOs ranking it their top priority. Significantly, some 35 per cent of CFOs would prefer to invest strategically abroad, with 8 per cent choosing overseas financial investments, an increase of 4 percentage points since the last survey.

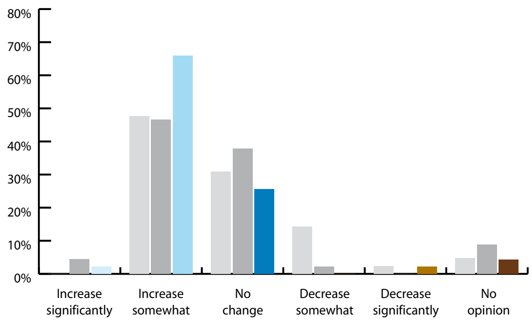


11. How do you currently rate valuation of Swedish companies?



Interestingly, CFOs now regard Swedish companies as slightly overvalued, an appreciable change compared to the fall survey. The OMX Stockholm 30 Index surged to record highs at the beginning of this year, both by index value and price to earnings ratio. However, with low interest rates and abundant market capital, the stock market may develop more positively than fundamentals indicate. Dividends and yields remain at reasonable levels.

12. Over the next 12 months how do you expect levels of corporate acquisitions and divestments in Sweden to change?



M&A activity has continued to increase in recent quarters with further improvements expected. Respondents are even more optimistic concerning numbers of M&A transactions compared to the fall survey. Some 68 per cent of CFOs now forecast increased activity. While M&A volumes remain well below historical levels, based on current developments, more companies are actively screening the market for potential acquisitions. We therefore still expect more transactions over the next 12 months, a view supported by respondents' increasing interest in strategic investments and their positive view concerning the lending attitudes of financial institutions.

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An international outlook

Easing uncertainty improves optimism

The most recent Deloitte CFO surveys in the UK/ Europe, North America, and Asia Pacific (conducted in Q4 2013) included the following findings:

Europe

- Across much of Europe, positive sentiment concerning local economies and business prospects has become more certain this quarter, while uncertainty has eased considerably.
- Some 80 per cent of Swiss CFOs are optimistic about their country's economic outlook, the highest share since March 2011.
- An overwhelming 96 per cent of Irish CFOs believe their economy has either returned to growth already or will do so in 2014.
- Dutch CFOs are more optimistic about their prospects than they have been since Q4 2010.
- In the UK, a record 57 per cent of CFOs say this is a good time to take risk onto the balance sheet, with business optimism higher than at any time in the last three-and-a-half years.
- The largest UK companies regard financing conditions as benign, as shown by the low cost and high availability of credit. In addition, CFOs expect all forms of capital raising – issues of bonds and equity, and bank borrowing – to increase in 2014.
- In Belgium, credit availability continued to increase in Q4 2013, and is still thought cheap by the average CFO.
- UK CFOs also place greater emphasis on capital spending, with 88 per cent expecting M&A activity to increase over the next 12 months. The Corporate Expansion Index has reverted to levels last seen in early 2011, when the UK looked set for sustained recovery.
- Dutch CFOs are still positive towards the M&A market. Meanwhile, they regard the private equity market bullishly, posting their most optimistic score (86 per cent) since Q1 2011. Some 92 per cent of CFOs expect the corporate M&A market to improve over the next 12 months.

North America

- CFOs in North America were generally optimistic in 2013, with strong Q4 results bringing the year to a positive end. Some 54 per cent believe their companies' prospects are improving (up from 42 per cent last quarter), while 21 per cent are more pessimistic, down from 24 per cent.
- While 82 per cent of CFOs expect increased sales, on average they expect a rise of only 4.1 per cent this year, the slowest rate since Q2 2010
- Nevertheless, some 55 per cent of CFOs expect the economy to be stronger in a year, while only 7 per cent think it will be worse (up from 2 per cent).
- Monetary policy concerns have escalated, with more CFOs expressing worries over the effects of "quantitative easing" and its eventual wind-down.
- Some 17 per cent of CFOs say their boards have faced pressure to return cash, while the same proportion of respondents state they are concerned by the actions of activist investors.
- Capital spending growth expectations fell sharply to just 4.9 per cent during the third quarter of last year, before recovering to 6.4 per cent in Q4 2013. Still, this is well below the survey average of 8.6 per cent (though manufacturing is relatively positive at 8.4 per cent).

Asia/Pacific

- CFOs in Asia Pacific are cautiously optimistic this quarter.
- Overall, 44 per cent of respondents in Southeast Asia say they were more optimistic in Q4 2013 than in the previous quarter. However, public companies are slightly more pessimistic, due to various macroeconomic factors including financial and economic uncertainty.
- Almost 60 per cent of Indian CFOs consider a slowdown in the domestic economy as an economic concern, followed by rupee depreciation and volatility.
- In Australia, CFOs regard issuing equity as far less attractive than the previous quarter. Meanwhile, 44 per cent of respondents see credit as either slightly or very cheap (compared to 42 per cent in Q3), while 78 per cent describe credit as moderately or easily available (up from 76 per cent in Q3).
- In Southeast Asia, CFOs are currently much more involved in risk management practices than 12 months ago. Due to changes in external and internal environments faced by companies, some 72 per cent of CFOs polled say they are more engaged in risk management than they were a year ago, while only 6 per cent claim to be less involved.
- The outlook for Australian M&A activity has improved significantly since respondents were last polled. At the end of last year, some 30 per cent of CFOs said their companies had more important matters to address than M&A activity.

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About the survey

The CFOs who responded represent a selection of the 200 largest companies in Sweden across industries. The survey was carried out as a web-based questionnaire in February 2014. Given the broad range of industries and organisations that responded, the trends observed and conclusions made are considered representative of the wider Swedish CFO community.

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