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SURVEY: CFOs THINK PRESIDENT BUSH SHOULD FOCUS ON IRAQ AND BUDGET DEFICIT; CONCERNED ABOUT HEALTH CARE COSTS AND INCREASING COMPETITION

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DURHAM, N.C. -- Chief financial officers of U.S. corporations are less bullish about the economy in 2005, and are particularly concerned about health care costs and operating in an increasingly competitive economic environment. They also rank the budget deficit and Iraq at the top of a list of items on which President Bush should focus during his second term. And executives at 36 percent of companies report that fears about domestic terrorism are significantly affecting their bottom lines.

These are some of the findings of the Duke University/CFO Magazine Business Outlook survey, which asks chief financial officers from a broad range of public and private companies about their economic projections. The December survey was concluded Dec. 5 and generated responses from 308 executives.

The survey asked executives to choose the top four items, from a list of 12, on which President Bush should focus his attention during his second term. More than two-thirds of the CFOs believe that addressing the U.S. budget deficit should be at the top of the president's list, while another 65 percent think the situation in Iraq should be one of the president's top priorities. Health care costs, social security and tax code reforms, and homeland security are other top priorities; each was chosen as one of the top four items by about 40 percent of the executives.

"This is a tall list of priorities that demand the president's attention," said John Graham, professor of finance at Duke and director of the survey. "But several notable items do not rank as priorities. Fewer than one-fourth of CFOs believe that the president's top priorities should include improving relations with allies, the trade deficit, the weakness of the U.S. dollar or high oil prices. Lack of concern about high fuel prices carries through to corporate activities, as only one in five of the companies we surveyed has implemented strategies to reduce fuel consumption."

The survey also asked executives to choose the top four risks to their companies during 2005, again out of a list of 12. Two-thirds of CFOs list health care costs as one of their top concerns, and another 56 percent list intense competition as one of their fears. Concern about operating in an increasingly competitive economic environment is greater for firms that have fewer foreign sales, so the threat appears to be particularly strong among domestic-focused companies, Graham said. Slightly more than 40 percent are concerned about the price of fuel and rising interest rates.

"Concerns about domestic terrorism have declined since last quarter, but our business terrorism index shows that the possibility of an attack is hurting business results," said Don Durfee, research editor of CFO Magazine. “We asked the CFOs to rank on a scale from 0 to 100 the negative impact that the threat of terrorism is having on their bottom line (where zero means no impact and 100 indicates maximum negative impact). While the terrorism index currently stands at 19.4, 36 percent of firms say the threat of terrorism is significantly affecting their bottom line.”

After robust growth this fall, employment gains appear to have stalled. CFOs expect employment to grow only 0.8 percent in 2005, down from 3.1 percent predicted last quarter. Also, health care costs are expected to rise 8.4 percent.

Despite these concerns, the survey results indicate that the bottom line should fare moderately well next year, with earnings expected to increase by 11 percent. Moreover, just over half of the executives say they are more optimistic about the economy, and their firms, than they were last quarter.

“All of these numbers are down from last quarter, and other predictions are even less favorable,” noted Graham. “Capital spending is expected to grow only at a ‘replacement level’ of 3.8 percent, and tech spending will increase just 4.9 percent. Worse still, the CFOs say that advertising and marketing expenditures will rise by only 2.3 percent, which is less than half of the growth predicted in last quarter’s survey.

“In addition, outsourced employment is expected to rise at more than half of the firms we surveyed, with the increase in outsourced employment expected to increase 4.3 percent. Finally, CFOs are significantly less bullish than Wall Street about the prospects for economic growth: respondents forecast a GDP growth rate of 2.8 percent, compared with Wall Street’s consensus forecast of 3.3 percent.”

The survey also inquired how much employees should expect from year-end bonuses this year. The average bonus will exceed last year’s by about 10 percent -- and will represent about 11.5 percent of annual wages. Although the average bonus will increase, it will be bigger at only about half of companies. Bonuses will decline at one-in-five firms.

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Among the industries represented in the survey are retail/wholesale, mining/construction, manufacturing, transportation/energy, communications/media, technology and banking/finance/insurance. Revenue-weighted mean growth rates are provided for earnings, revenues, capital spending, technology spending, and prices of products. Employee-weighted mean growth rates are used for health care costs, productivity, number of employees and outsourced employment. Except as noted, the results presented herein are for the full sample of 308 respondents. The numbers for earnings, revenues, capital spending, technology spending, health care costs, number of employees and outsourced employment are for public firms only.

Detailed results of this survey, as well as other outlook surveys, are available at <http://www.cfosurvey.org>.

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