



INSTITUTE FOR BUSINESS IN SOCIETY

Views from the C-Suite:

*Aligning Stakeholder Interests
With Corporate Strategic Decisions*

BY

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The Darden Institute for Business in Society (IBiS) held its Strategic CFO Roundtable on 25 September 2014 in Arlington, Virginia. The first half of the session was spent discussing members' views of the U.S. economy and the performance of their own businesses. The second half of the Roundtable is reserved for a Top of Mind Topic that serves as an in-depth discussion for the CFOs. For this Roundtable, we asked the CFOs to discuss the tradeoff of long term profits with specific resource decisions related to the operations of their company.

The week prior to the CFO roundtable, Janet Yellen, the chair of the Fed, announced that the Fed's policies of continued low interest rates and the end of quantitative easing were still in place. The announcement was largely anticipated, but nevertheless was greeted with enthusiasm by the stock market as the Dow closed at 17,156, a record high. The Treasury bond market also reacted positively as the 10-year bond yield fell to 2.58 percent (down 3 basis points). For the most part this positive sentiment was reflected amongst the Roundtable participants who reported solid performances for their companies and a continued optimistic outlook for both the economy and their own companies.

THE SURVEY

Prior to each Roundtable session, we conduct a survey to provide insights into the business views of the Roundtable Members in the Washington D.C. Metropolitan Area relative to their counterparts nationwide. We compared the survey results of the Roundtable Members to a separate national survey, Duke University/CFO Magazine's Global Business Outlook Survey, which has polled senior finance executives over the past 74 quarters. The survey responses prompted conversation among the Roundtable Members regarding their expectations of domestic and global economic recovery, the financial condition of their own firms and evidence of recent actions for growth of their companies.

Economic Outlook

The September 2014 Darden IBiS Strategic CFO Roundtable Survey showed a continued level of optimism regarding the U.S. economy that exceeded the levels reported in the national survey. The graph below depicts how CFOs rated their optimism about the U.S. economy on a scale of 0 – 100%. (See Figure 1) Both the national Global Business Outlook and the Darden IBiS Strategic CFO Roundtable Survey reported optimism levels over 60%.

The national survey (solid line) rose slightly from 61% for Q2 2014 to 63% for Q3 2014 while the Roundtable Member CFOs (dashed line) exhibited a noticeable decline from 64% for the Q2 2014 survey to 57% for the September 2014 survey. A closer look at the data reveals that two of the six CFOs responded below 50%; i.e., to suggest a lack of optimism about the U.S. economy. The rest of the responses signaled various levels of optimism with the highest response being 80%.

Figure 1: Optimism for the U.S. Economy
 (Scale of 0 – 100%)

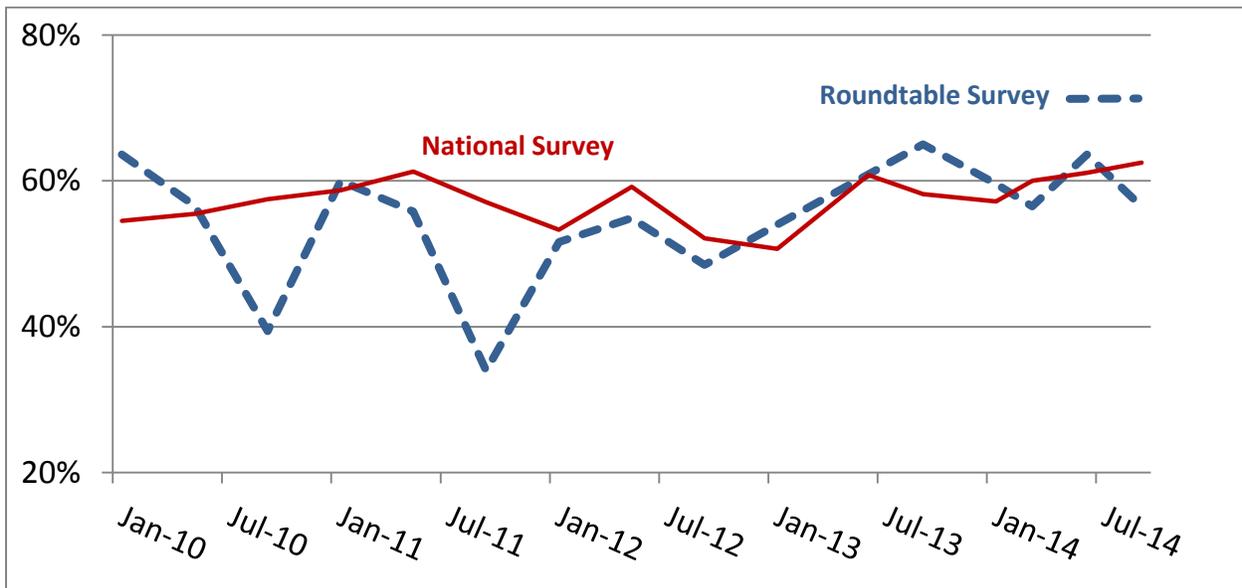
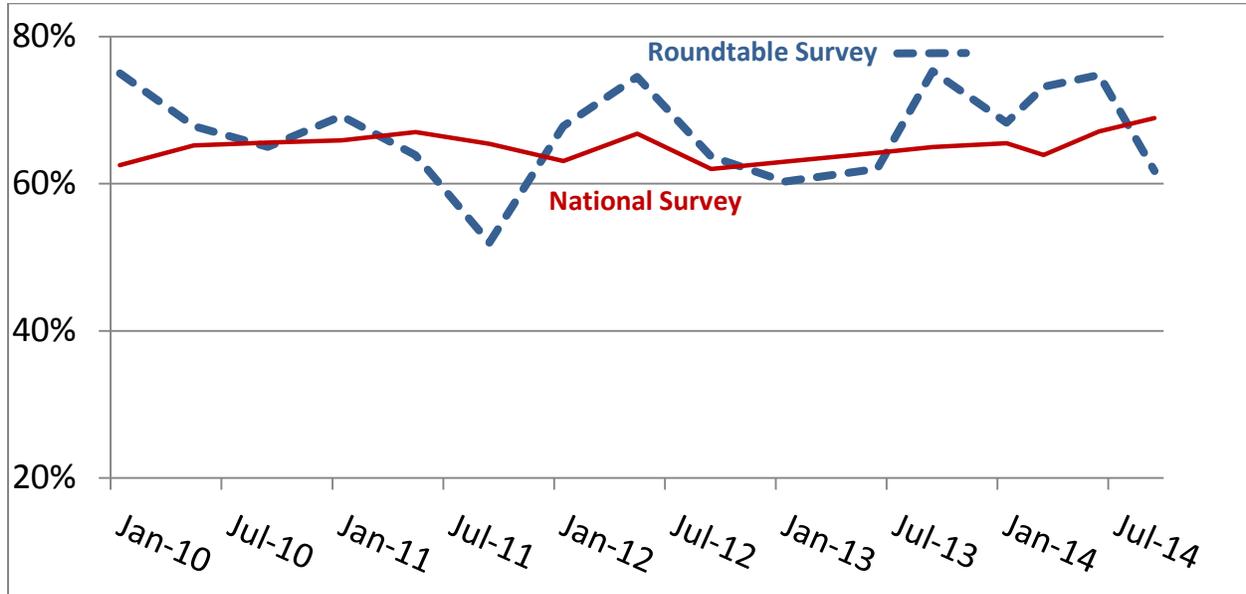


Figure 2 compares the CFO Roundtable group with the national survey regarding their optimism about their own companies. Historically both of these surveys have consistently reported higher levels of optimism for their own companies relative to the U.S. economy and the Roundtable optimism for “own company” has frequently been higher than those reported by the national survey. For the September survey, however, we see lower optimism levels (dashed line) for the Roundtable CFOs relative to the national survey (solid line). As in the past, most of the CFOs expressed higher optimism about their own companies with the average of 62% exceeding by 5% (57%) the optimism reported by the CFOs for the U.S. economy. The CFOs for the national survey report a premium of 6% for their own firms (69%) vis-à-vis the U.S. economy (63%). On average, our Roundtable members have reported a premium level of optimism for their own company of about 13% since 2010, compared to an 8% premium reported by the national survey.

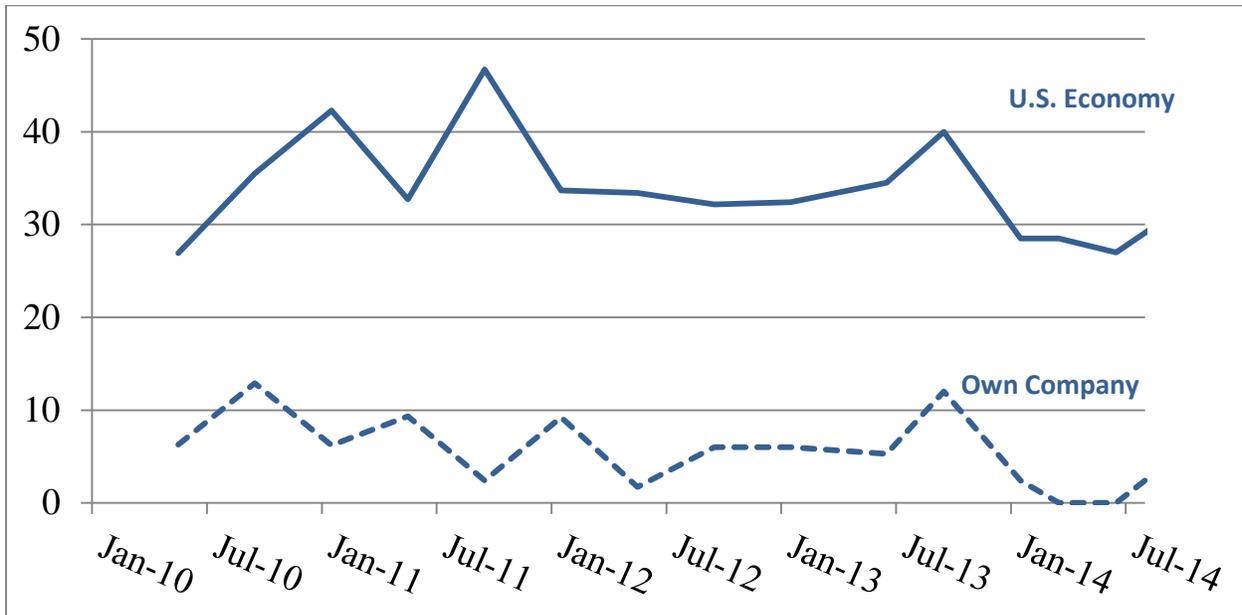
Figure 2: Optimism for their Own Company
 (Scale of 0 – 100%)



Employment

Since its inception, the Roundtable Survey has asked participants to estimate the number of months that will pass before domestic employment will return “to pre-crisis (year end 2007) levels for the U.S. economy.” The solid line in Figure 3 reveals that Roundtable Members’ expectations have consistently been between 30 and 40 months for the past couple of years. The level dropped to 27 months for the June survey, but rebounded to 31 months for the September survey. One CFO responded “never” for the U.S. economy question. Such a response could not be meaningfully included in the calculation of the average, and therefore, a fair interpretation would best be, “For those CFOs who believe the U.S. unemployment will eventually return to pre-crisis levels, they expect it to take two to three years.”

**Figure 3: When Will the U.S. Return to Pre-crisis Employment?
 (Months)**



The dashed line in Figure 3 reflects the Roundtable Members’ optimism about the employment levels of their own companies. The CFOs have consistently viewed their own company employment levels as much better than the overall economy. As for many of the recent surveys, the responses for the September survey were mostly zero months; i.e., they had already returned to pre-crisis employment levels. One CFO response was omitted from the average, because he reported that his company would “never” return to the pre-crisis employment level. On balance, it is fair to say that most of the Roundtable CFOs see their own company employment as having fully recovered since the onset of the recession in 2008, with a minority reporting the scale of their company will remain smaller than before the crisis.

TOP of MIND TOPIC

The Top of Mind Topic was generally concerned with how CFOs make decisions and specifically, how CFOs balance profits with resource decisions related to the operations of the company. The survey asked the following question: “Relative to your competitors, how do you rank your company’s investment level for the attributes listed below? [Employee Wages, Employee Benefits, Information Technology, Property, Plant and Equipment]”

	Lowest Quintile	Below Average	Average	Above Average	Highest Quintile
Employee Wages			33%	67%	
Employee Benefits			17%	50%	33%
Information Tech			40%	40%	20%
PP&E			50%	33%	17%

The responses reveal that our CFOs take a market viewpoint for deciding these “investment levels”. All responses are at or above “Average”. Assuming that the average represents a competitive level, all of the CFOs strive to be competitive in their respective markets. For benefits, IT and PP&E, the CFOs often see themselves as offering among the very highest levels of investment. Being at the highest end of the investment spectrum goes beyond the competitive response level, but nevertheless was seen by the Roundtable participants as offering enough payoff to merit the extra cost.

As an example, a frequently cited benefit of higher wages and benefits was the ability to attract and retain the best talent. On the issue of compensation, one CFO emphasized the effort put toward benchmarking compensation:

[For] wages, we have a philosophy and we benchmark every position. And every position in the organization has a target comp ratio. Some of them are around median comp and some areas are 75th percentile, so blended average, we are above median. But some areas of the company ... we want to be within 90 percent to 105 of median ... and then some positions we want to be around the 75th percentile and so there’s a lot of thought that goes into it.

The general consensus among the Roundtable CFOs was that compensation is always important to employees, but if given the choice, employees would tend to react more favorably toward a premium benefit package than a premium wage. This is consistent with 33% of the Member companies offering benefits in the highest quintile. As the members shared their compensation practices in more depth, they discussed their providers of benchmarking data and how they used the data for compensation decisions. The discussion about the specific information available through the different providers prompted a couple of CFOs to think about adding a new provider to take advantage of a new set of data.

Related to the decision process were a couple of topics that had surfaced recently in the press. The first came from a CFO magazine article¹ based on a survey of 1,135 executives. Seventy-nine percent of the executives reported that they make a “big” decision every quarter. One third of the execs defined the value of their decision as \$1 billion or greater. The execs reported a high reliance upon data for decision making and yet only 32% considered their process to be “highly” data driven. The Roundtable CFOs were not surprised at the 32% number, which was consistent with previous Roundtable discussions about an “intuitive ROI”; i.e., the need to go with intuition for many difficult decisions.

The second survey result discussed was from the national survey; i.e., the Duke University/CFO Magazine’s Global Business Outlook Survey for Q3 2014. The survey asked, “Have you considered changing your firm’s country or state of incorporation to reduce your tax obligations?” of the 378 respondents, 50 (13.2%) replied “yes”. The Roundtable CFOs were surprised at this number, which they viewed as very low. The CFOs surmised that the answer would depend upon the interpretation of the word “considered”. There was agreement that this sort of possibility should be considered by every CFO, if only at the very basic level of the *potential* value that could be created for shareholders. In fact, rather than the 13% reported, the Roundtable CFOs were guessing a level of 80% or higher of CFOs would have thought about the value of a tax inversion. However, if “considered” were interpreted as making a presentation to the board, then they viewed 13% as a high number.

One CFO summarized his firm’s view of tax inversion as: “... we’ve considered that [but] we’ve ruled it out simply because we have a fair amount of our business tied up with the government.” Another member stated, “I would say we’ve considered [it], but it’s so low value, a very little bit of effort went into the consideration before we ruled it out. But, I would have put us as a yes [for] considering different ways of leveraging international tax structures.” The consensus at the table appeared to be that virtually every value-adding strategy is “considered” at some level, but only a few survive the early analysis to advance to serious thought.

The Darden IBiS Strategic CFO Roundtable will re-convene Thursday, 8 January, 2015.

¹ “Execs Still Make Big Decisions with Their Gut: Study”, Iris Dorbian, CFO Magazine, September 27, 2014.
<http://ww2.cfo.com/leadership/2014/09/execs-still-make-big-decisions-gut-study/>

About the Author

Kenneth M. Eades, Professor of Business Administration, is the Chairman of Darden Finance Department and serves as Interim Academic Director for Darden's Richard A. Mayo Center for Asset Management, as well as Associated Faculty with the Darden Institute for Business in Society. The author of numerous academic articles, more than 50 Darden cases and three books, Eades has received both research and teaching awards.

About the Darden IBiS Strategic CFO Roundtable

The Strategic CFO Roundtable is a quarterly, invitation-only convening of leading chief financial officers in the Washington D.C. Metropolitan Area to discuss, debate and share best practices on enhancing the strategic role of the CFO. With over 300 years of strategic financial and leadership experience, the Roundtable participants share their views on the challenges and opportunities facing their companies. They discuss the lessons learned from triumphs and trials that led to their becoming recognized as strategic CFOs. The Strategic CFO Roundtable is organized by the Institute for Business in Society at the Darden School of Business of the University of Virginia.

About Darden Institute for Business in Society

The Institute for Business in Society (IBiS), established at the Darden School in 2011, prepares leaders to positively impact society through business. IBiS advances thought leadership and innovative practices through research, teaching and programs.

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Darden IBiS Strategic CFO Roundtable Survey Results

September 2014

	N = 6 Public RT Sept 2014		N = 6 Public RT June 2014		N = 6 Public RT Mar 2014		N = 7 Public RT Jan 2014		N= 379 Duke Q3_14		N= 400 Duke Q2_14		N= 375 Duke Q1_14	
	Average	Median	Average	Median	Average	Median	Average	Median	Average	Median	Average	Median	Average	Median
1. Compared to last quarter, are you more or less optimistic regarding- U.S. economy (Less =1, More = 3)	1.8	2.0	1.8	2.0	2.0	2.0	2.4	2.0	2.2	2.0	2.2	2.0	2.2	2.0
1. Compared to last quarter, are you more or less optimistic regarding- Financial prospects for your own company (Less =1, More = 3)	2.0	2.0	2.2	2.0	2.5	2.5	2.4	2.0	2.3	2.0	2.3	2.0	2.2	2.0
2. Rate your optimism regarding: (Drag the slider to assign a number.)- U.S. economy	56.5	57.5	63.6	66.0	56.5	60.0	59.6	62.0	62.5	65.0	61.1	60.0	60.0	60.0
2. Rate your optimism regarding: (Drag the slider to assign a number.)- Financial prospects for your own company	61.7	62.5	74.8	75.5	73.2	70.0	68.3	70.0	68.9	75.0	67.1	65.0	63.9	70.0
4. Regarding domestic employment, when do you anticipate a return to pre-crisis (year end 2007) levels for the U.S. economy -Months	31.2	36.0	27.0	24.0	28.5	33.0	28.5	27.0						
4. Regarding domestic employment, when do you anticipate a return to pre-crisis (year end 2007) levels for your firm -Months	4.8	0.0	0.0	0.0	0.0	0.0	2.4	0.0						
5. How would you rate...-Your employees' morale level ? (Poor =1, Satisfactory =3, Excellent = 5)	3.7	4.0	3.8	4.0	4.2	4.0	4.0	4.0						

Darden IBiS Strategic CFO Roundtable Survey Results

September 2014 (Continued)

	N = 6		N = 6		N = 6		N = 7	
	Public RT Sept 2014		Public RT June 2014		Public RT Mar 2014		Public RT Jan 2014	
	<u>Average</u>	<u>Median</u>	<u>Average</u>	<u>Median</u>	<u>Average</u>	<u>Median</u>	<u>Average</u>	<u>Median</u>
(Weaker =1, No change = 2 Stronger = 3)								
6. Recent quarter's financial results vs. previous quarter: -Income Statement	2.2	2.0	2.3	2.5	2.5	2.5	2.6	3.0
6. Recent quarter's financial results vs. previous quarter: - Balance Sheet	1.8	2.0	2.2	2.0	2.7	3.0	2.4	2.0
6. Recent quarter's financial results vs. previous quarter: - Cash Balance	1.7	1.5	2.2	2.0	2.4	3.0	2.4	3.0
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8. Expected change over the next 4 quarters vs. last 4 quarters: - Income Statement	1.9	2.0	2.3	2.5	2.7	3.0	2.8	3.0
8. Expected change over the next 4 quarters vs. last 4 quarters: - Balance Sheet	1.9	2.0	2.3	2.5	2.7	3.0	2.5	2.5
8. Expected change over the next 4 quarters vs. last 4 quarters: - Cash	1.9	2.0	1.7	1.5	2.4	3.0	3.0	3.0
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(Reduced =1, No change = 2, Higher = 3)								
9. Expected change over the next 4 quarters vs. last 4 quarters: - Headcount	2.3	3.0	2.2	2.5	2.3	2.5	2.7	3.0
9. Expected change over the next 4 quarters vs. last 4 quarters: - Capital Spending	2.0	2.0	1.7	2.0	2.2	2.5	2.4	3.0
9. Expected change over the next 4 quarters vs. last 4 quarters: - Compensation	2.0	2.0	2.2	2.0	2.2	2.0	2.7	3.0
9. Expected change over the next 4 quarters vs. last 4 quarters: - Pro develop/training	2.0	2.0	2.0	2.0	2.2	2.0	2.3	2.0
9. Expected change over the next 4 quarters vs. last 4 quarters: - Prob (new mkt/product)	1.8	2.0	2.3	2.0	2.2	2.0	2.4	2.0
9. Expected change over the next 4 quarters vs. last 4 quarters: - Prob (Acquisition)	1.7	2.0	2.2	2.0	2.0	2.0	2.0	2.0