CFOs' Fuel Fears Rise to Join Consumer Worries

Anxiety is high among finance chiefs in the United States, Europe, and Asia in the new Duke University/*CFO* study. But glimmers of optimism may be starting to shine through.

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Soaring fuel costs have joined sagging consumer demand in a virtual tie as top concerns of CFOs, according to the latest Duke University/*CFO* magazine Global Business Outlook Survey.

It is the first time that fuel costs have risen to that level, equaling the consumer related worries that for several quarters have been the top plague of finance chiefs. And in the face of rising oil-related bills, finance executives are not standing by passively.

Nearly half of the firms polled in this second-quarter survey say they would begin to pass fuel-cost hikes through to customers by raising prices. And those prices are expected to go up by 4.1 percent in the next year, partly as a result of fuel pass-alongs.

CFOs don't expect the economy to turn around until mid-2009, and 40 percent of those surveyed expect to reduce, delay, or cancel investment plans during the next six months.

Most companies are taking other defensive measures, too, to ward off the effects of record-high oil prices. A third of CFOs in the survey say their firms have shifted to more efficient shipping methods, while 45 percent are raising prices, another 45 percent are reducing business travel, and 43 percent have made their facilities more efficient. A quarter of the CFOs say they have seen their profit margins shrink due to higher fuel costs, and 13 percent have taken to using financial derivatives to hedge against further increases.

CFOs are seriously concerned that the impact of pricey oil will seep into the far corners of the economy and be a drag on growth. "This could be the longest slowdown since the double dip recession of 1979-81," says John R. Graham, director of the survey and a finance professor at Duke's Fuqua School of Business. "Even more worrisome, there is evidence of stagflation — slow economic growth and rising unemployment combined with inflation."

Of the 1,051 CFOs surveyed this quarter, 71 percent say they did not expect the economy to rebound until 2009, and 54 percent did not expect a rebound to happen until the midpoint of the year. As a result, U.S. companies expect to reduce their domestic workforces by an average of 0.2 percent this year. Capital spending is expected to increase by just 2.3 percent, and earnings growth will rise by an "anemic" 2.9 percent, according to the survey's producers.

Persisting Credit Woes

Although the mushrooming credit crisis this year has receded in the minds of some CFOs, many firms — particularly those with lower ratings — are still feeling credit-related pain. Credit remains hard to find, say 58 percent of CFOs. Half of those polled say borrowing costs have increased and nearly 60 percent say they will have to reduce investment or hiring as a result.

"The bad news is that the credit crisis is devastating lower-rated firms," according to Duke Professor Campbell R. Harvey, the founding director of the CFO survey. "Eighty-two percent of these companies have been hurt directly by the credit crunch."

On the bright side, CFOs show somewhat less pessimism than they displayed in the previous quarter, despite the generally gloomy environment. After several quarters of declining optimism, 53 percent of CFOs say they are more pessimistic about the U.S. economy this quarter, and 21 percent say they are more optimistic. In the last survey, released in March, optimism reached a six-year low. At that time, 72 percent of finance chiefs were more pessimistic about the U.S. economy than they were the quarter before, while 8 percent felt more optimistic.

"This quarter, we're seeing bad news with a little bit of good news," Harvey says. "In the fourth quarter of 2007 and the first quarter of 2008, pessimists outnumbered optimists by an 8 to 1 margin. This quarter, the ratio has improved to roughly 3 to 1, potentially indicating stabilization."

The View from Abroad

Pessimism is spreading among CFOs globally, the survey suggests. In Europe, 64 percent of finance chiefs are more pessimistic about their domestic economies compared to the previous quarter, while just 8 percent are more optimistic. Meanwhile, employment in Europe is expected to fall by 1.2 percent, capital spending is expected to increase by 2.8 percent and earnings will rise by 3.1 percent, according to the survey. Weak consumer demand and the cost of fuel are the top two concerns among European CFOs, as well.

In Asia, CFO optimism has reached a new low, with 62 percent feeling more glum about regional economic growth and 21 percent feeling better about it compared to the previous quarter. However, optimism in Asia still trumps that in Europe or the U.S. Employment in Asia is expected to rise by 3.3 percent in the next year and CFOs expect to increase capital spending by 6.7 percent and increase wages by 6.2 percent.

Asian CFOs are also reporting growing signs of the region's economy "de-linking" from that of the U.S. Among finance chiefs polled in Asia, 35 percent say the current slowdown in the U.S. has not hurt their firms and 27 percent say that any negative impact is less than it would have been five years ago. Of those who have been negatively affected, 71 percent say the slowdown has led to reduced customer orders, and 40 percent say customers are demanding price discounts.