KPMG

CFO Outlook Survey

March 2017

Nigeria

KPMG CFO FORUM

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Foreword

The KPMG Chief Financial Officers (CFO) Forum is a platform for discussing issues of common interest to CFOs and creating an avenue for CFOs to interact as a group with relevant government regulators and policy makers. The Annual CFO Outlook Survey is one of our levers for achieving this objective.

The Nigerian economy has been adversely affected by external shocks, in particular, a fall in the global price of crude oil, compounded by the over-reliance on crude sales as the main source of foreign exchange earnings in a highly import-dependent economy.

As we look for nascent signs of an economic recovery, we sought the views of CFOs on the outlook for their businesses in 2017, their current strategies for cost and risk management and what they believe the priorities of government should be for the creation of an enabling environment.

In terms of outlook, respondents were generally less optimistic about the prospects for growth in 2017 when compared to 2016. The top three 'stay awake' issues for our respondents are foreign currency availability and exchange rate volatility, operational challenges exacerbated by weak infrastructure and inconsistent government policies. These are indeed tough times and the corporate results released thus far are reflective of the difficulties being experienced. It is interesting to note however that the same respondents expressed significantly more optimism when asked about growth prospects over a two to three year horizon. This medium term optimism may be indicative of expectations of an imminent upturn in the economy possibly based on the cumulative impact of turnaround measures being put in place by the Federal Government. Policy consistency and a strong focus on implementation by Government will go a long way in providing the certainty needed to improve and sustain business confidence.

In dealing with the present challenges, CFOs have had to adopt various strategies to ensure their businesses survive these times. Most of these strategies are focused on improving service delivery, strengthening customer acquisition and loyalty and redesigning operations to improve efficiency and reduce costs. Our respondents reported that risk management is a key priority for them with the top three risks being currency risk, liquidity risk and credit risk. For sustainable results, it is important that company's risk management strategies are based on a well thought through financial risk management framework rather than a 'seat of the pants' approach. CFOs must use risk management to improve results, optimally allocate resources, protect organisational assets and achieve growth. The ability to seize business opportunities is often heavily dependent on the ability of the CFO and other members of the C-suite to identify, assess and manage risks.

Nigeria is currently ranked 169 among 190 economies in the `Ease of doing business' index published by the World Bank. Raising Nigeria's ranking on the index is a stated priority of Government. The ease of doing business parameters that our respondents believe require priority action from Government are; getting

electricity, getting credit, starting a business and trading across borders. Our respondents were also clear that in dealing with the current challenges, the most important priorities for Government should be infrastructure development and foreign exchange policy review.

Our gratitude goes to all the CFOs who took out time out of their very busy schedules to complete the survey. Your contributions to this year's survey have been instructive and quite revealing. There is no doubt that the skills and experiences required of CFOs today is very different from those that were required five years ago and these skill requirements will continue to evolve.

We hope you find our 2017 CFO Outlook Survey Report insightful and replete with insights that can be adapted in various forms for the benefit of your organisations.

Where there are specific themes and messages you want to explore further, I urge you to get in touch with any of the contacts listed on the last page of this Report. For us at KPMG, we remain committed to providing a platform for articulating critical issues of concern to CFOs and actively participating in the dialogue between CFOs and Government.

" CFOs must use risk management tools to improve results, optimally allocate resources, protect organisational assets and achieve growth. The ability to seize business opportunities is often heavily dependent on the ability of the CFO and other members of the C-suite to identify, assess and manage risks."

Tola Adeyemi
Partner & Head
Audit Services
KPMG in Nigeria

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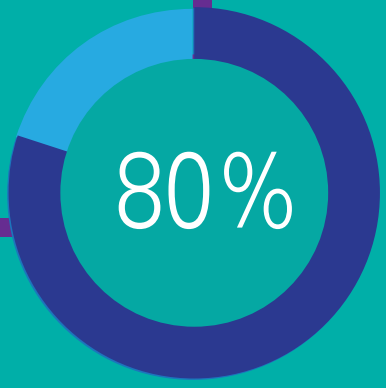
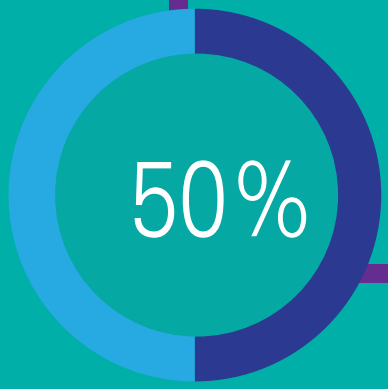
Growth Prospects in 2017

CFOs are more pessimistic about the prospect of growth in 2017 compared to 2016. 64% of respondents are either less confident about the country's economic outlook or are of the opinion that it will remain the same.

Direction of Nigerian Economy

CFOs are cautiously optimistic about the direction of the Nigerian economy over the next 3 years. 80% of respondents believe that the Nigerian economy will be better than it is at present, but still below its potential over the next 2-3 years.



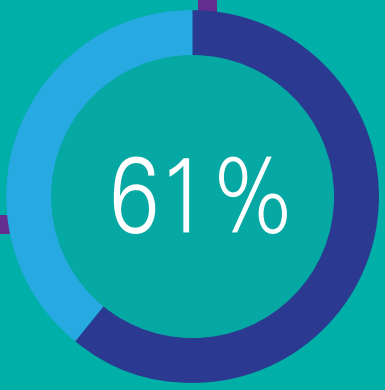


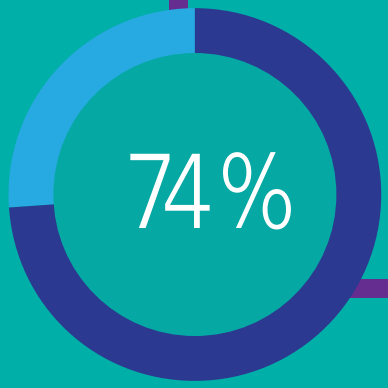
"Stay Awake" Issues

In this year's survey, half of CFOs identified foreign exchange availability & currency volatility as the most important 'stay-awake' issue for them, closely followed by operational challenges arising from poor infrastructure.

Area of Spend for Future Growth

Sixty-one percent of CFOs believe that service delivery is a major influencer of growth for their organisations. Customers are at the heart of the growth strategy of most companies.



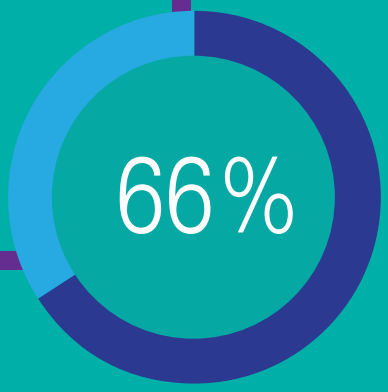


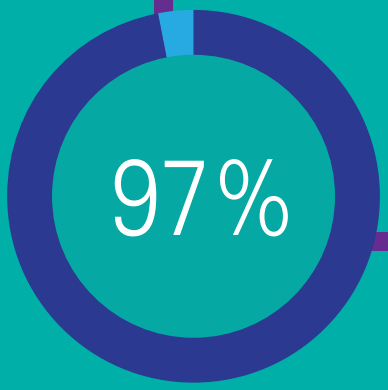
Managing Exchange Rate Risks

Seven out of ten CFOs are managing exchange rate risk in their organisations by mitigating with risk management instruments and seeking local alternatives to foreign inputs.

Techniques for Responding to Current Conditions

Cutback/ Delay on CAPEX ranked as the top business defensive strategy that 66% of CFOs rely on in responding to current economic conditions. Delayed CAPEX investments will likely constrain future growth potentials of organisations, or delay how quickly businesses can respond when growth eventually returns.



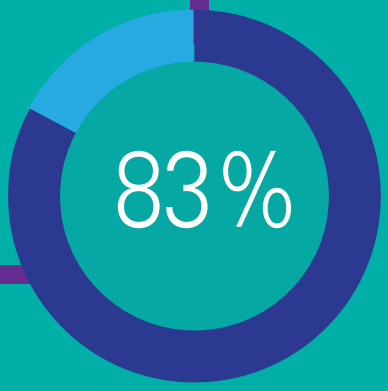


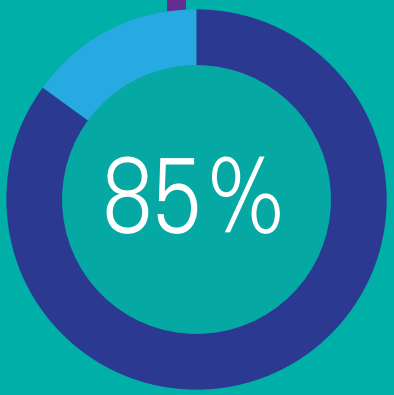
Benefits of Additional Assurance

Managing financial risk (credit risk, liquidity risk, currency risk and interest rate risk) is a major area of concern for almost all of the CFOs and they believe they require additional assurance in this area to ensure that risks are properly managed.

Ease of Doing Business in Nigeria - Priority for Govenrment

A significant majority believe that solving the power problem in Nigeria would be a major catalyst for any expected growth over the next few years. 83% of respondents consider the provision of reliable electricity to be a major priority for government.





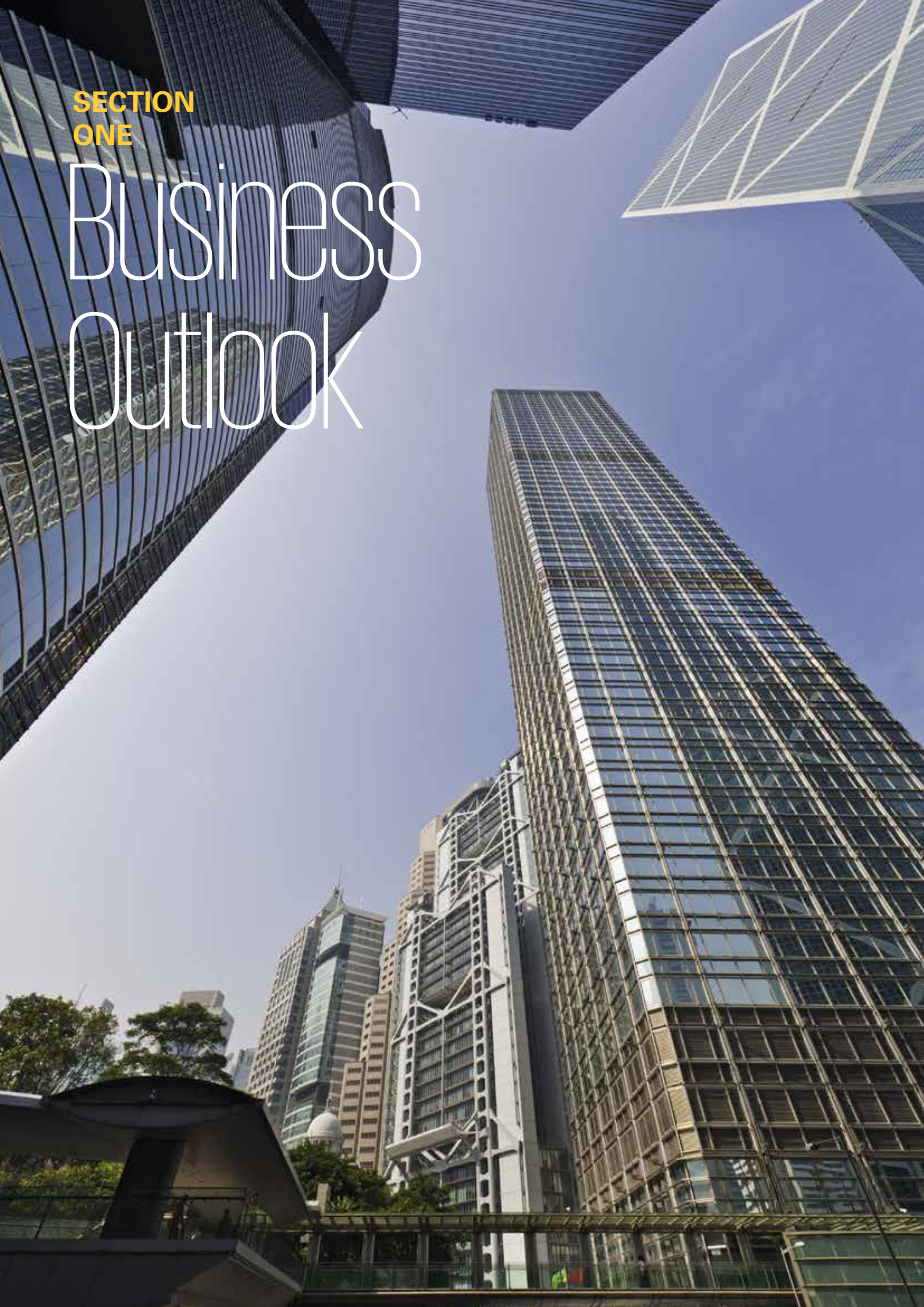
Areas for Government Support

An overwhelming number of respondents will like to see improved government support in terms of exchange rate policies, as a major spur for the growth prospects of their industry/ organisation. The second major area of priority for improved government support is infrastructure development.

Source: 2017 CFO Outlook Survey, KPMG in Nigeria

SECTION ONE

Business Outlook



Nigeria's economic performance worsened in 2016. The economy was severely affected by the plunge in crude oil prices, decline in oil production, and the reduction in non-oil exports, all of which contributed to the acute scarcity of foreign exchange. The National Bureau of Statistics (NBS) released the GDP numbers for Q4-2016 recently. Real GDP contracted by -1.3% y/y, showing fourth consecutive negative growth y/y. Although the decline was less severe than the contraction recorded in the previous quarter (-2.2% y/y), it compares less favourably to the 2.1% growth recorded in the corresponding quarter of 2015.

Although economic activity is showing some faint signs of improvement, conditions remain challenging and weakness persists at the outset of the year. These concerns were expressed by credit rating agency, Fitch, which downgraded the country's outlook to Negative from Stable. Fitch expressed concern that the lack of FX liquidity could stifle a meaningful recovery, and rising interest costs just as the country is tapping into international bond markets to finance an aggressive fiscal policy to stimulate growth.

As a result of the above, it became necessary to seek the views of the CFOs on the Outlook for their business, highlights of their views are presented below;

Q1 How confident are you about the prospects for growth for next year (2017) compared to this year (2016)?

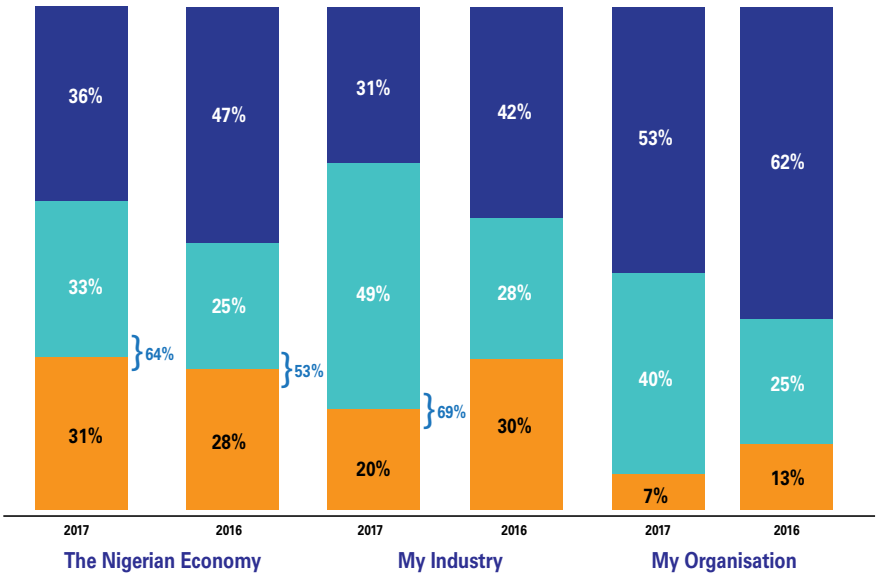
KPMG INSIGHT

Business confidence is an important indicator of the state of the economy. It provides an overview of the satisfaction of businesses with prevailing conditions. Given the decline of this indicator over the recent past, it is pertinent that both business leaders and government focus on short – medium term strategies to protect value and enhance growth

CFOs are more pessimistic about the prospect of growth in 2017 compared to 2016. 64% of respondents are either less confident about the country's economic outlook or are of the opinion that it will remain the same.

The turmoil in the Nigerian economy over the last 12 – 18 months has resulted in an even greater number of CFOs (69%) who are either less confident of growth in their industries or expect current conditions to remain the same.

The harsher realities faced within the operating environment is responsible for the waning optimism of CFOs in their company's growth prospects. Only 53% of CFOs in this year's survey (compared to 62% last year) indicated that they were confident in the growth prospects of their organisations in 2017.



Source: KPMG Analysis

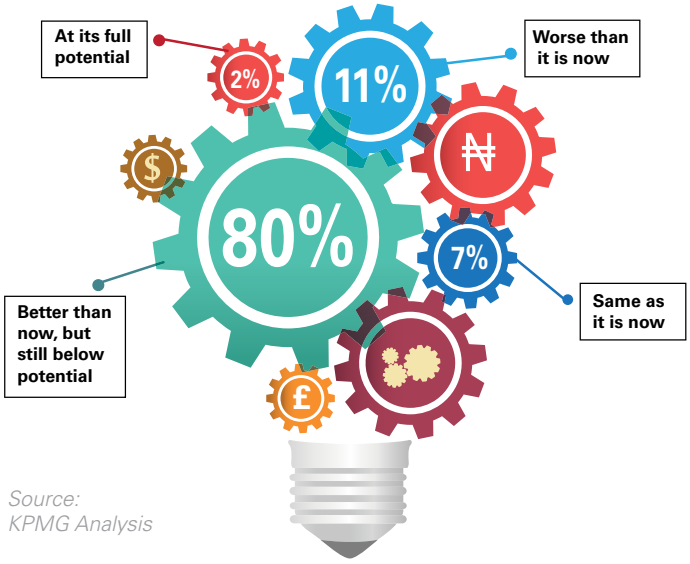
Q2 In the next 2-3 years, what direction do you see the Nigerian economy tending towards?

KPMG INSIGHT

Despite the current strain In the economy, the outlook for the medium term still appears optimistic. Government needs to do all it can to sustain this medium term optimism.
Optimism can be seen as an essential ingredient of innovation. Some believe it is the single most important factor to a business success with a strong correlation between an optimistic economy and increased opportunities.

CFOs are cautiously optimistic about the direction of the Nigerian economy over the next 3 years. 80% of respondents believe that the Nigerian economy will be better than it is at present, but still below its potential over the next 2-3 years.

However, a significant number of respondents expressed concerns over the medium term direction of the Nigerian economy, with 18% of respondents of the view that the economy will either remain as it is or become worse.



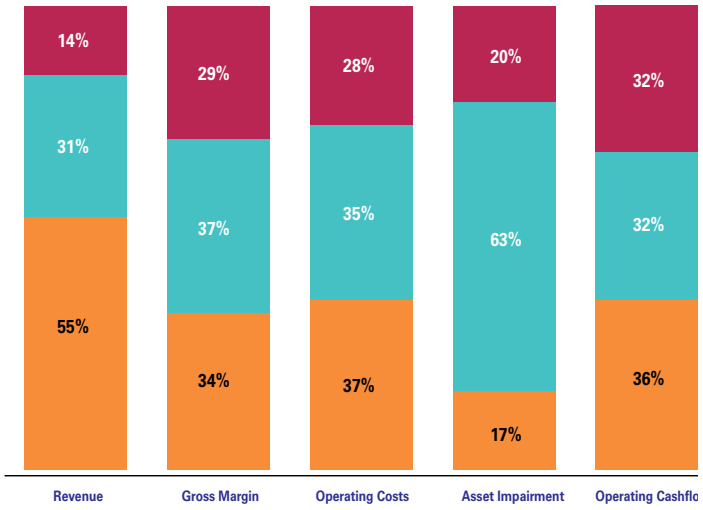
Source:
KPMG Analysis

Q3 In your opinion, how are the following metrics for your organisation likely to change over the next 12 months?

KPMG INSIGHT

Improved revenues pre-supposes an increase in commodity prices or quantities sold. This, in a receding economy, may only be achievable where innovation and 'out of the box' strategies are effectively deployed by companies. With a combination of other measures such as cost optimisation, effective asset deployment and cashflow management, companies may be able to turn a surviving business into a thriving one.

Compared to 2016, CFOs were generally optimistic on improving or sustaining their Revenue and Operating Costs metrics but less so for Gross Margin and Operating Cashflows. CFOs also provided responses on a new metric this year – Asset Impairment, 80% of them were very positive in their expectations that this metric will either be sustained or improve over the next 12 months. This could be reflective of the fact that impairment hits taken in 2016 were already factored in the outlook for 2017.



Source:
KPMG Analysis

Q4 As the CFO of your organisation, what are your top three 'stay-awake' (most important) issues?

KPMG INSIGHT

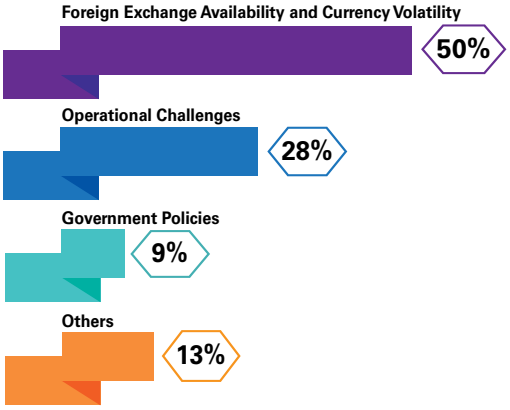
The poor state of the nation's infrastructure, coupled with the highly volatile foreign exchange regime and constantly changing government policies, have burdened business leaders with enormous challenges to keep them awake. Navigating these challenges in the current economic environment is certainly not 'business as usual'. It requires an extraordinary level of focus on long-term drivers of sustainable value creation.

In this year's survey, CFOs identified foreign exchange availability & currency volatility as the most important 'stay-awake' issue for them, closely followed by operational challenges arising from poor infrastructure.

This view by CFOs is unsurprising given the negative impact that exchange rate volatility and weak infrastructure have had on the economy and operations of businesses.

Government Policies ranks third but may arguably be the major driver for the first two issues. The clarity and execution consistency in government's policies, rules and regulations, usually provide a guide to businesses.

The absence of the right signals from government will have a negative impact on the competitiveness and profitability of companies.



Source: KPMG Analysis

Q5 To what degree are the following factors a likely impediment to your organization's growth and profitability in the next three years?

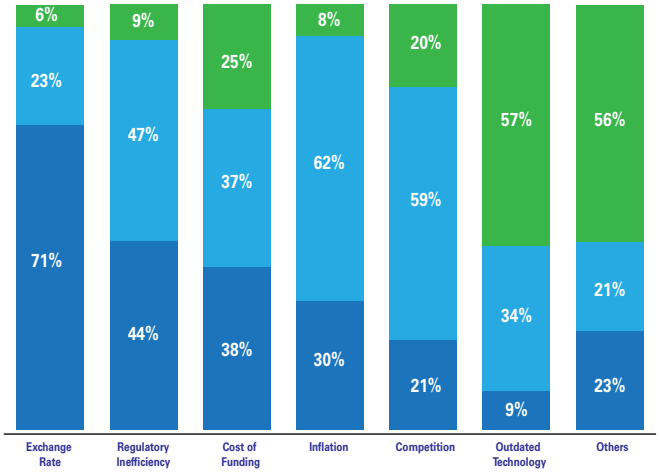
KPMG INSIGHT

The volatility of the exchange rate regime causes significant disruptions to the planned activities of companies. It is therefore important for companies to embrace risk management tools to help hedge against potential adverse effects this could have on profitability and growth.

Foreign currency availability and exchange rate volatility continues to inflict havoc on businesses. This factor appears to pose the most risk to organisations' growth and profitability in the next 3 years as 71% of CFOs indicated that it represented the greatest hurdle.

A significant number of CFOs also remain wary of Regulatory Inefficiency and Cost of Funding, with 44% and 38% of respondents respectively considering these factors to be high impediments.

Overall, the major factors that are ranked high by CFOs as barriers to growth and profitability appear to be mostly external to the companies and outside their control.

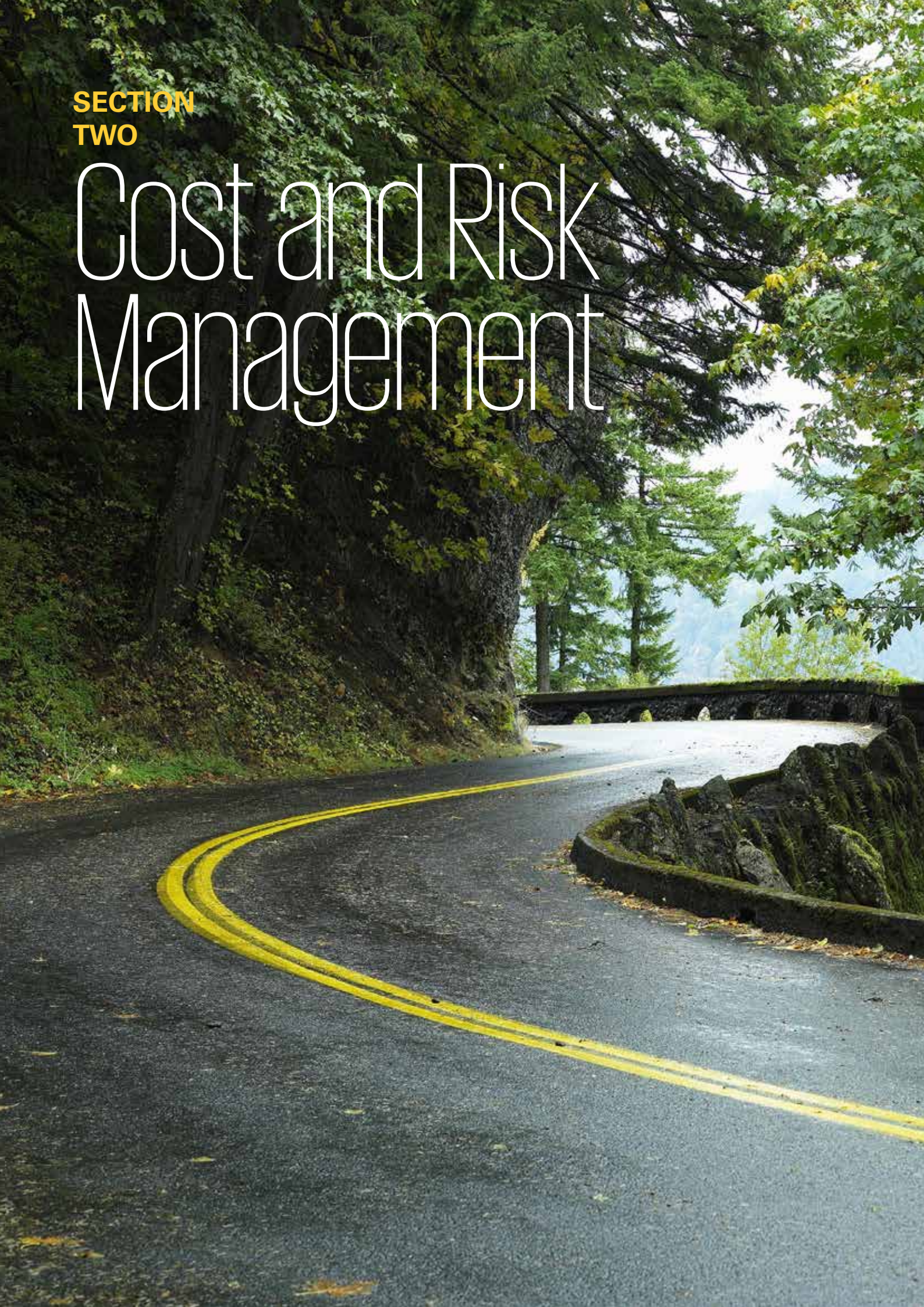


Source: KPMG Analysis

High Impediment (1&2) | Average (3-5) | Low Impediment (6&7)

SECTION TWO

Cost and Risk Management



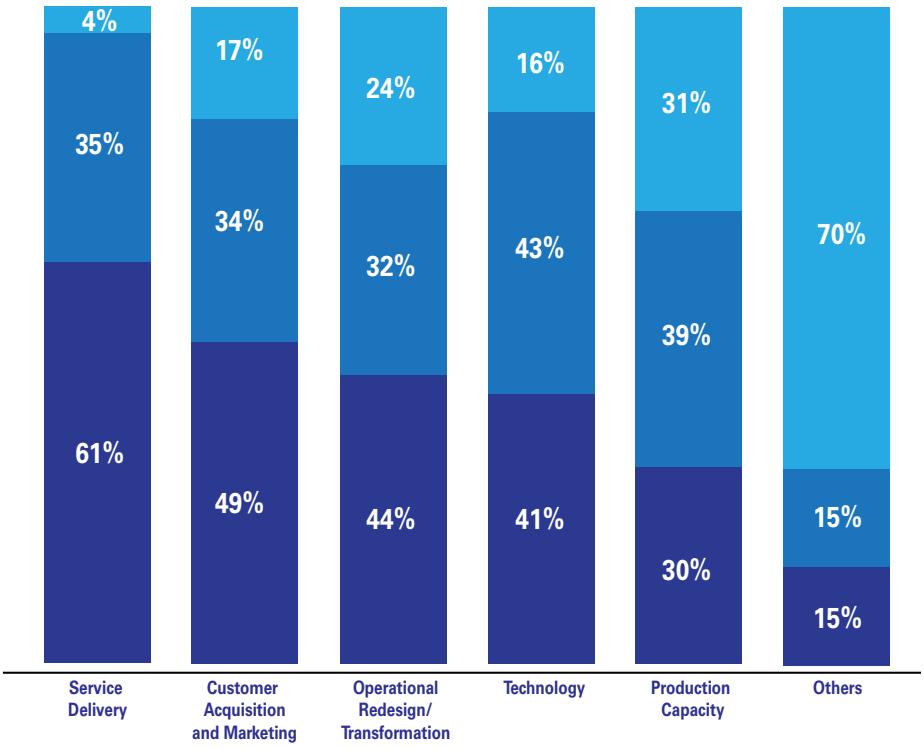
Q6 Where will you be spending the most to influence future growth of your organisation?

KPMG INSIGHT

With the widespread availability of data in many businesses, we have reached a point where leading organisations significantly leverage the power of analytics in the most important decisions affecting their business. Data on Service Delivery and Customer are some of the areas that have been benefiting from increased analytical attention in recent time.
Industries with an extensive retail focus are mining existing internal and external data, and throwing up insights to drive more targeted interventions to enhance service delivery and prevent customer churn among other objectives.
In our view, Data & Analytics is a major factor that is and will continue to underpin competitive advantage. Among other objectives, it helps to know customers better, streamline existing businesses more efficiently and manage risk and compliance on a more general basis. Organisations that ignore the power of data & analytics will only realize when the market must have moved.

It is instructive that 6 in 10 CFOs see Service Delivery as a major influencer of growth in their organization. This validates KPMG's findings over the last 10 years, that shows that service is the major driver for a customer in choosing and maintaining relationships.

Closely following this, about 5 in10 CFOs also indicated that their companies will be investing in Customer Acquisition and Marketing to drive future growth.



Source: KPMG Analysis

"The customer is at the heart of the growth strategy of most successful businesses. Companies will likely continue to make strategic investments for the acquisition, servicing and retention of customers"

Segun Sowande
Partner & Head
Management Consulting
KPMG in Nigeria

Enhancing Business Decisions with Data & Analytics

Due to the historical focus on transaction cycles, the finance and accounting departments have the best access to organizational data. And though finance has traditionally brokered an understanding of performance, the function also manages the transactional data that tracks performance throughout the organization. So who better than financial executives to organize the data, make it ready for mining and translate it to significant value? CFOs are in a prime position to create a data-driven intelligent enterprise. By taking charge of data governance and business analytics, CFOs are the best suited to identify opportunities for value and apply stronger discipline throughout the entire organization.

With the widespread availability of data in many businesses, we have reached a point where leading organisations significantly leverage the power of analytics in the most important decisions affecting their business. Whether it relates to customer, service delivery, product development, asset utilization or other operational areas, data is being used to discover hidden patterns underlying performance in specific areas, and influence decisions that yield the maximum impact for the business.

As the member of the C-suite that sits on most of the data in the organisation, the CFO needs to evolve beyond the finance function to identify value across the broader enterprise, providing insights to help the rest of the organization improve performance and manage risk along various dimensions of the business.

CFOs have access to a wealth of data from ERP systems, line-of-business applications, and management reporting tools. Armed with this keen understanding, CFOs are sitting on a goldmine of information that, with the right management and analytics, can be translated into performance insight and meaningful value that produces more accurate decisions on customers, service delivery, product development and other business enablers. In essence, the CFO can see the bigger picture, make truer forecasts, and pave a clearer path to value—by partnering with the business units to improve strategy, operations, IT, supply chain, sales, and marketing, while deploying capital more intelligently.

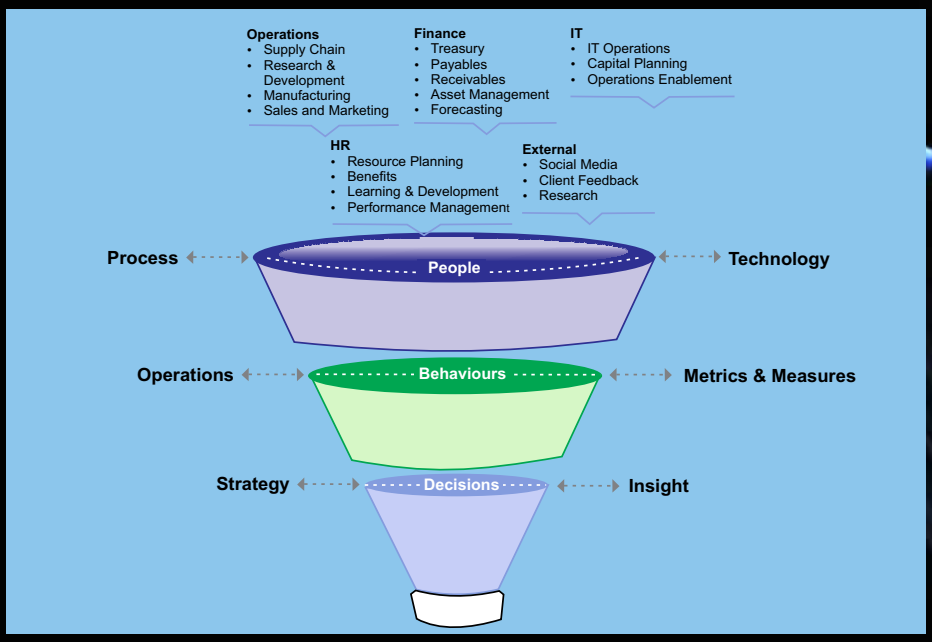
Improving business intelligence

A key differentiating role for the CFO is driving the connection between operational and financial performance. For example, a common manufacturing priority is managing the efficiency of plant utilization and capacity. But plant throughput also has direct ties to revenue forecasts, and the CFO can integrate manufacturing analytics to drive the connection. It comes down to identifying a wider variety of levers for managing overall business performance. With expanded influence as the steward of information management, CFOs can go beyond finance to identify opportunities for growth and cost savings across regions, functions, and the enterprise as a whole.

Leading enterprises use business analytics to accelerate business performance. They manage corporate data as a differentiating asset, with a focus on both horizontal and vertical integration of enterprise resource planning (ERP) systems, operational data stores, data warehouses and appliances, reporting systems, analytic engines, and more. These organizations evaluate business intelligence as a corporate competency—with discipline around people, process, and technology—and they embed analytics as a strategic tool for smart business decisions. They no longer see analytics as just a series of reports with different views; they instead speak of multiple dimensions and data cubes. They think in hierarchies, and they insist on clear metadata ownership and management as part of generating, managing, and utilising analytic tools.

> **"Tomorrow's competitive advantage will be driven by the ability to identify, consume, produce, and govern the complex information inside and outside the company's walls"**

It is the CFO who is leading this renewed focus on performance and risk management, and the CFO is demanding the right information at the right time to realize sustainable value. For example, some CFOs are working with business units to more effectively deploy capital. Others are reducing the



cost and delay of financing by freeing up working capital and deploying it more efficiently. Specifically, CFOs are leveraging business analytics to invest in the right growth areas and influencing strategic decisions based on analytics including product profitability, customer profitability, fraud analytics, working capital management and tax intelligence among others.

A 360-degree view

When information takes center stage, it can help organizations make better fact based decisions and create better processes. However, creating this new intelligent business model can be a significant change journey. An effective information-driven approach should apply historical, current, and predictive analytics to give organizations a 360-degree view of their data. This view enables a focus on business outcomes and measurable value. More organizations are also incorporating customer analytics, including customer sentiment (which stems from external data), and they're integrating these risk indicators as part of the holistic view of business performance.

While the data itself is an asset, the real opportunity is turning that data into value—in the form of growth, cost savings, and other benefits across the organization. CFOs can help the company harness its data in a program that includes data governance analytics, benchmarking, reporting, leading practices, and intimate knowledge of the business strategy.

> **" Leading enterprises use business analytics to accelerate business performance. They manage corporate data as a differentiating asset "**

Data analytics can improve decision-making throughout the business, helping organizations unlock value by:

- Identifying new market opportunities
- Improving responsiveness to customers, based on a greater understanding of their needs and satisfaction with products and services
- Increasing strategic relevance of the workforce by understanding employees' motivations and aspirations
- Improving financial discipline and integrating business performance across operations, supply chain, manufacturing and logistics
- Identifying better ways of measuring and managing risk.
- Optimizing operational performance through transparent fact based analysis

As organisations roll out initiatives to enhance the value of their business, the use of data (internal or external) and analytics will go a long way in enhancing the value of decisions, and more importantly ensure that the organisation is deploying its resources to its most productive areas .

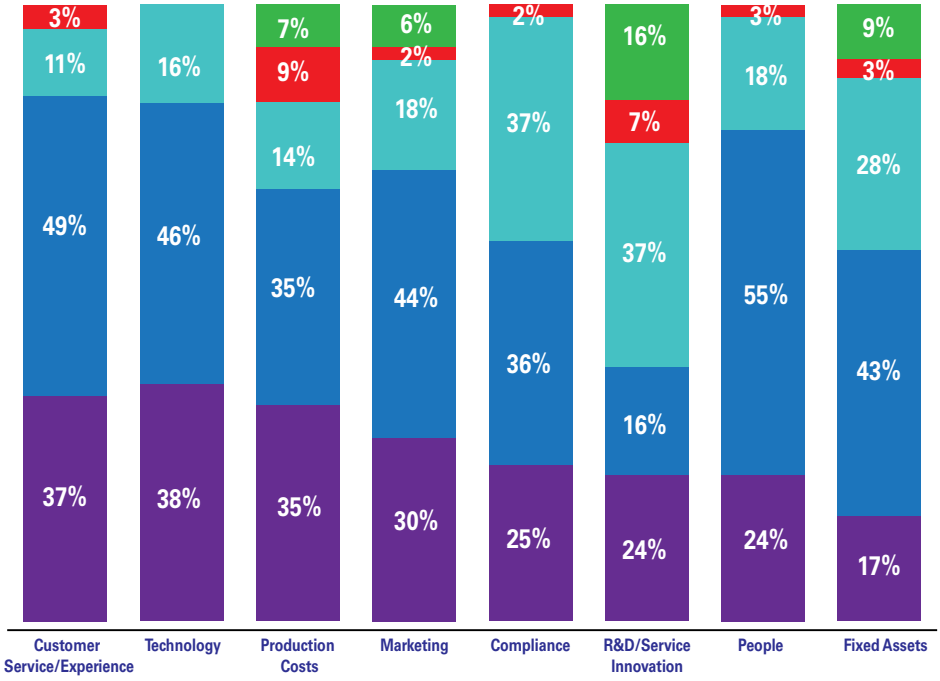
Q7 How will costs change in the following areas of your business over the next three years?

KPMG INSIGHT

With increasing competition comes the need for organisations to innovate and reinvent themselves as well as their products and service offerings. No wonder significant resources are deployed to investment in research and development. Technology can transform several aspects of a business and is a veritable catalyst for growth and expansion.

The recognition of technology as a major driver of innovative service delivery and customer acquisition is underpinned by the fact that about 8 out of 10 CFOs believe that costs will increase in the area of Customer Service/Experience and Technology over the next 3 years. 38% of these respondents expect a major increase in Technology spend over the same period.

The importance of research and service innovation, as a platform for competitiveness and differentiation to businesses, is captured by the sentiments of CFOs. 79% of respondents expect their organisations to increase spend in this area in the next 3 years.



Source: KPMG Analysis

Major Increase | Minor Increase | No Change | Major Decrease | Minor Decrease

Avoiding the Cost Rebound Trap

As we highlighted in the 2016 edition of the CFO Outlook survey report, when faced with margin pressures, businesses often implement rapid and broad cost-cutting measures – slash and burn exercises. While this approach may yield short-term gains, it is only a matter of time before such costs boomerang into the business.

While growth prospects remain uncertain in the current economic clime, many organisations are already facing the challenge of mounting costs quickly eroding their already tight profit margins and eliminating bottom line growth. Today, businesses that are able to identify and exploit sustainable cost-efficiencies will enjoy significant competitive advantages over their peers: better profit margins, more flexible working capital and a greater alignment for future growth. Those that aren't, however, seem destined to remain at the mercy of the economy, doomed to a cycle of market driven cost-reductions and reactive, knee jerk survival strategies.

The Cost Rebound

Under pressure from the macro-economic headwinds, most companies looked for quick-hit cost-cutting measures that would immediately maintain profit margins and sustain the bottom line. Most companies have not implemented the more radical and sustainable cost efficiency measures and as a result, the hard-earned cost savings are now being exposed as largely unsustainable with sizeable chunks of these costs returning into the business in the short-term.

Executive Management needs to maintain strong cost disciplines and gain a stronger understanding of where value is generated within their organisations. They can then ensure that additional costs are only invested in the strategic priorities of their businesses.

Sources of Costs

Where will costs rebound back into the business? The simple answer is everywhere.

Understanding the sources of potential cost increases is a critical first step in creating a more sustainable cost environment, allowing organisations to take a longer-term view of cost management. While some of these costs – particularly those stemming from external forces – may be impossible to mitigate, C-suite Executives that are able to achieve a clear vision into the cost base will be better prepared to eliminate costs that are either unnecessary or are not aligned to the company's future growth strategy.

Driving Sustainable Cost Efficiency

Why are costs prone to returning so quickly? Most believe it is because past cost cutting measures were conducted unsustainably.

If Executive Management is really serious about reducing its organisation's cost base and making reduction sustainable in the long-term, then it must be prepared to challenge the accepted business model orthodoxy which underpins everything the business does. To truly achieve this, the C-suite will need to take a different perspective on their organisations. If not, the pervasive inability to see beyond long-held operational constraints will continue to restrict businesses' ability to make real inroads into their cost base. Without objectively challenging the embedded ways of working, businesses are limited in the scope they have to make substantive changes in areas which could deliver real cost efficiencies. This is especially true for organisations that have been forced through a number of rounds of cost efficiencies, as many are reaching the laws of diminishing returns within their current operational constraints.

> **" Understanding the sources of potential cost increases is a critical first step in creating a more sustainable cost environment, allowing organisations to take a longer-term view of cost management."**

Stripping out costs is hard work. And while those that lose focus may well still achieve growth, it may be unprofitable growth. But those that persist with cost as a Board-level strategic concern will create space within which to grow their margins and secure a real competitive advantage.

Embedding a Cost Culture

Any cost management effort that isn't adopted by the employees is destined to fail. So it is critically important that all employees – from the frontline workers

through to senior management – are aligned in the cost management process. Creating a cost culture is about more than mandated measures and top-down initiatives. It requires everyone in the business to be fully engaged, cost-conscious, and pulling in the same direction.

In part, this will require organisations to instil a greater sense of ownership within their middle-manager and frontline staff. It will be critical for these employees to have a clear understanding of the commercial operations of the business so that they understand how their role fits into the overall strategy of the business, and where they can affect positive change in the cost base of the business.

Our experience reveals that the traditional methods of rewarding employees may be over-rated as a way of eliciting culture change. Instead, companies should try to ensure that organisation structures are based on establishing clear accountabilities and decision rights. This should ensure that accountability for cost is not 'syndicated' to the point where no one is actually accountable. More powerful still is to instil a sense of ownership into the employee base which will drive improved performance right through the organisational hierarchy.

It will also be vital for organisations to create robust and effective tools and mechanisms to support employee innovation and awareness. To achieve this, management will need to work closely with frontline staff and middle managers to form a better understanding of the types of tools and level of information that is required to properly activate employee engagement. Put simply, without feedback mechanisms that give visibility to the progress that the organisation is making in terms of cost and value creation, then sustainable cost management will always remain an aspiration.

In almost every situation, organisations that embed a culture of cost consciousness are significantly better positioned to identify and leverage sustainable cost management opportunities and ultimately avoid the cost rebound trap. But creating a cost culture is not always easy. In most cases, it will require a fundamental rethink about how employees view costs and how they are empowered and rewarded for making sound cost management decisions.

Conclusion

Clearly, there is an urgent need for companies to place a greater emphasis on cost efficiency and an increased cost consciousness in order to drive competitive advantage and survive in a slowing economy. For many C-suite Executives, this process will, by necessity, begin with a careful analysis of the existing cost drivers of the organisation in order to increase their understanding of where value is created and profit is generated.

To do this, organisations must be prepared to look across divisions and business units, compare themselves through robust competitive benchmarks that not only look at numerical comparisons but also highlight alternative ways of working, and then make some tough decisions which may challenge the accepted business models and transform their internal culture.

The cost rebound trap is undeniable and organisations that do not take firm and sustainable measures to stem the flow will likely soon find themselves dealing with ever tightening profit margins and a stagnant bottom line.

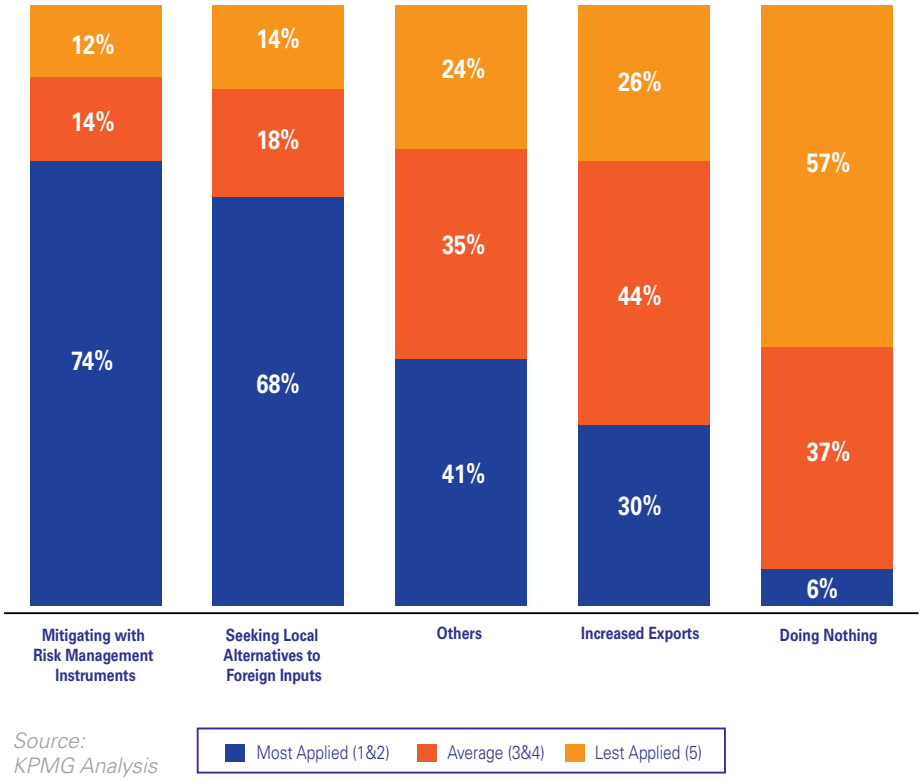
Q8 How are you managing exchange rate risk in your organization?

KPMG INSIGHT

In managing foreign exchange risk, organisations can do the following:

- *Identify and quantify existing exchange risks using a variety of leading practice metrics*
- *Model potential impact from exchange rate volatility on earnings and revenue*
- *Identify potential hedging instruments and methods to effectively mitigate price volatility (e.g., options, swaps, forwards, futures, and non-derivative financials)*
- *Analyze hedging instrument feasibility considering expected hedging costs, benefits, and aggregate corporate exposures at-risk, cash-flow-at-risk, value-at-risk (VaR), expected shortfall stressed value-at-risk (sVaR) and other management information metrics*
- *Coordinate FX risk management design, drawing on extensive experience in developing comprehensive FX risk management frameworks, including infrastructure, hedging strategy, related processes, and risk oversight design*

CFOs appear to have largely adopted two major strategies to manage exchange rate risk: mitigating with risk management instruments (74%) and seeking local alternatives to foreign raw inputs (68%)



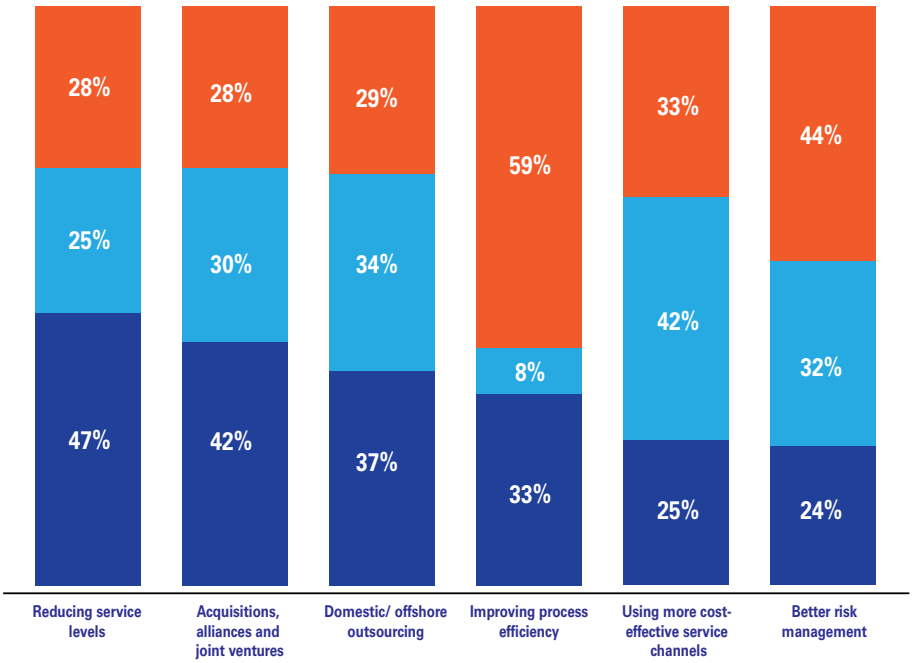
Source: KPMG Analysis

Q9 How important will the following strategies be as part of your cost management over the next three years?

KPMG INSIGHT

In light of economic, financial and regulatory pressures and in these turbulent times, cost management strategies are increasingly important in enhancing operational excellence, while simultaneously, businesses focus on improving service delivery. Business leaders are increasingly using various approaches to manage their costs – reducing service levels on non-critical activities, entering into alliances to share cost and outsourcing of non-core activities, among others.
It is important that successful cost optimization needs to be positioned beyond mere cost reduction, it needs to adopt a sustainability lens to ensure that cost cuts in one area of the business do not subsequently show up in another area of the business.

Reducing Service Levels, Acquisitions/ Alliances & JVs and Outsourcing (Domestic & Offshore) appear to be the top 3 cost management strategies for CFOs in the medium term, given the proportion of CFOs that have indicated these factors as either high or of average importance.



Source: KPMG Analysis

High Importance | Average (3&4) | Low Importance (5&6)

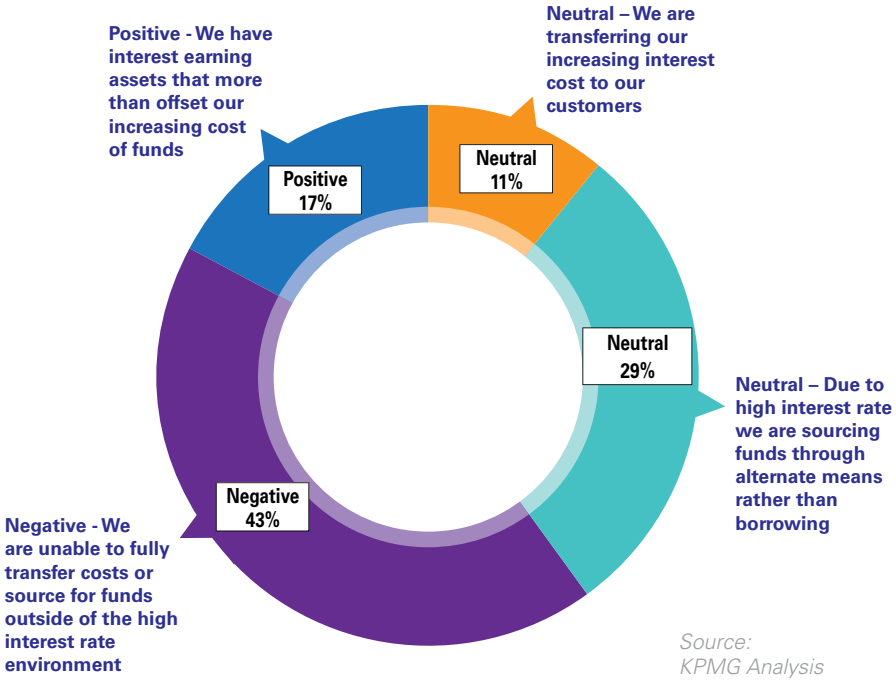
Q10 How are you affected by the interest rates in the current environment?

KPMG INSIGHT

As conventional credit markets get tighter, alternative finance sources are becoming increasingly important, and will gradually play a more important role in the corporate financing landscape. Organisations are leveraging non-debt financing, including recapitalization and release of working capital, to lower their cost of funds. In some other instances, more sophisticated finance functions rely on hedging instruments to manage their interest rate exposure. As innovation in the corporate finance market continues, it is increasingly imperative for CFOs to evaluate creative alternatives within the context of their organisations' financial and liquidity management needs. In addition to this, CFOs should evaluate the various financial risks in their portfolio, and develop proactive strategies to manage these risks on an overall basis.

The interest rate environment in the country has largely had a negative impact on businesses. This impact on business operations has been two fold: inability to transfer increased costs down the value chain to consumers, and increased difficulty in sourcing funds.

However, 17% of CFOs indicated that due to their investments in interest earning assets, they have witnessed a positive impact as the increasing cost of funds has been mitigated by higher interest income.



Source: KPMG Analysis

"When interest rate goes up the cost of borrowing increases. This reduces companies' profitability. It also tends to reduce consumer spending and investment."

Nike James
Partner
Tax Risk Management
KPMG in Nigeria

Q11

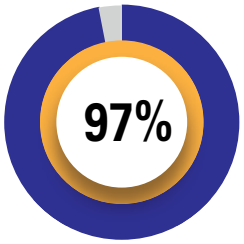
In which of the following areas do you believe your organisation will benefit from additional assurance that the related risks are being properly managed?

KPMG INSIGHT

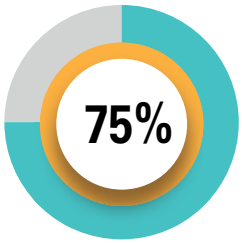
In order to cope with the various types of financial risks businesses are regularly exposed to, CFOs need to take an integrated view of their organisation's strategy, funding and liquidity risk. They also need to critically evaluate their financial risk management practices and develop effective scenarios to stress test the practices. Ultimately this will ensure adequate focus on the survival and success of the organisation.
Also, Regulatory and Tax compliance demand considerable focus. CFOs need to provide assurance that compliance management has been done correctly and efficiently across all tax and regulatory areas. The risk of back-duty exposures including penalties or fines, or even reputational damage, can be significant, and CFOs need to take active steps to ensure regulatory and tax risks are reduced to the minimum in their organisation.

Financial Risk appears to be a major area of trepidation for CFOs as 97% of respondents require additional assurance in this area.

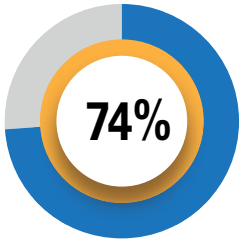
Other areas of significant concern for CFOs include Regulatory Compliance, KPI Measurement (the top concern in the last survey), Tax Risk and Internal Controls.



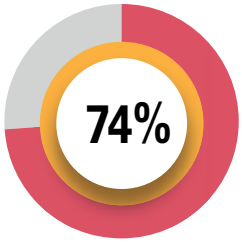
Financial Risk (Credit risk, Liquidity Risk, Currency Risk, and Interest Rate risk



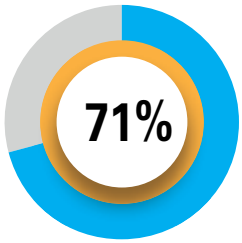
Regulatory Compliance



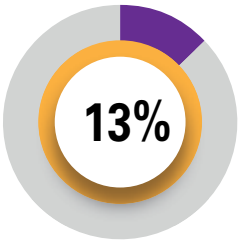
KPI Measurement



Tax Risk



Internal Controls over Financial Reporting



Others

Source: KPMG Analysis

The Role of Regulators in a Depressed Economy

On 31 August 2016, the National Bureau of Statistics (NBS) announced that Nigeria had entered into a recession[1]. According to the NBS, Gross Domestic Product declined by -2.06%, annual inflation rose to 17.1% in July from 16.5% in June, and food inflation rose to 15.8% from 15.3%.

The impact of the challenges posed by the recession is being felt both at the macro and micro levels. Nigeria, being largely import dependent, has witnessed a continuous depletion of its foreign exchange reserves. Also at the micro level, many organizations are unable to cope with rising operating costs, and are, therefore, compelled to scale down on their operations, leading to loss of jobs and income. There is no doubt that our economic challenges, as a nation, are multifaceted and require strategic regulatory interventions which may not be assessed independent of governance variables.

However, our regulators must rise to the occasion and embrace multi-dimensional and carefully coordinated initiatives in getting the nation out of its current predicament.

Below are some suggested actions for our regulators. These actions will help with the stabilization of the ailing economy in the short term and achieve the much needed sustainable economic growth in the medium term:

Embrace Collaborative Policy Making

The policies of the various regulators and ministries, departments and agencies of government should complement each other and should be targeted towards the same goal. For example, the monetary policy directives of the Central Bank of Nigeria must complement the fiscal policies initiatives of the Ministry of Finance and vice versa.

[1] A recession occurs when an economy records two consecutive quarters of negative GDP growth rate.

There must be a consistent story around the policies of various regulators which should tie into the overall policy thrust of the government.

Government must never be seen to be reversing itself due to policy inconsistencies, else investor confidence will continue to erode and the nation will be worse-off for it.

Create a Competitive Business Environment

Regulators need to consider the competitiveness of the global economic landscape in the formulation of policies. Consequently, our policies should be targeted at making the Nigerian business environment competitive to attract long term foreign investment.

Over the past six months, quite a few businesses have moved their regional hubs out of Nigeria owing to our business environment. We need to quickly stem this tide and work to attract more Foreign Direct Investment into the country.

Formulate Pro-Business Policies

Regulators need to be guided by the fact that businesses need to survive and indeed grow for the nation to emerge from recession.

Therefore the policies of the regulators especially during this period of recession need to be specifically designed to stimulate and support businesses activities.

This is the time to offer incentives, waivers and other forms of sweeteners for business who are ready to make long term investments in Nigeria, amidst the current challenges.

Manage the Revenue Generation Drive

Owing to the recession, most regulators are now working hard to be self-funding or, at the least, support the subvention received from the government.

Regulators, however, need to strike a healthy balance between the drive for revenue generation for government spending (which is encouraged during recession) and over levying the businesses that generate the revenue.

The policy decisions of our regulators especially our tax authorities as seen over the past few years, show a tendency for inconsistencies and controversies in the interpretation of the tax law. This is coupled with an aggressive revenue drive which clearly impacts negatively on the business climate. Regulators therefore need to adopt effective and efficient strategies to improve compliance levels and generate additional revenues, without adversarial consequences.

Our review of reforms, particularly tax reforms around the globe point to the need for our regulators to adopt a "risk-based approach" to compliance management, as the necessary solution to this challenge.

Based on the above, regulators definitely have an important role to play in getting the nation out of recession. Regulators must rise to this challenge and work as a team in leading the nation out of recession

Q12 In what order does your business rely on the following techniques in responding to current economic conditions?

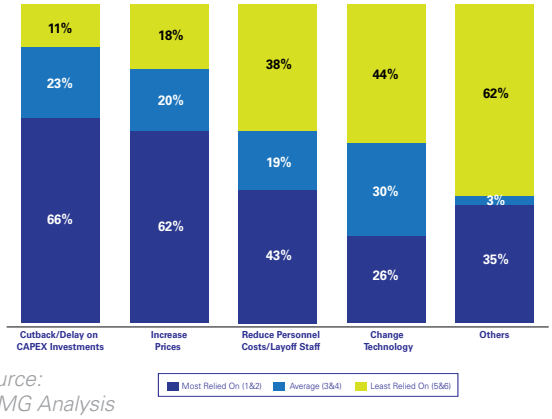
KPMG INSIGHT

The burden on CFOs has increased in recent years due to governance and regulatory challenges. It is clear that CFOs need to be more well-rounded, multidisciplined leaders with a strong line of thinking around business growth and shareholder returns. The CFO role has evolved in the last five years, mainly because of digitalization but also globalization in terms of operations, compliance, governance and control. A key differentiating role for the CFO is driving the connection between operational and financial performance. For example, a common manufacturing priority is managing the efficiency of plant utilization, capacity, and backlog. It is very clear that CFOs need to continually seek innovative ways to respond to the current economic conditions.

Cutback/ Delay on CAPEX and Price Increases ranked as the top two business defensive strategies for CFOs.

This scenario has future implications for both the businesses and the Nigerian economy. Delayed CAPEX investment will likely constrain future growth potentials of the organisations, or delay how quickly businesses can respond when growth eventually returns.

Price increases by businesses will likely dampen demand and continue to stoke the fires of inflation, in an environment already experiencing the highest levels of inflation in over a decade.



Source: KPMG Analysis

Q13 On a scale of 1 to 4 rank the following risks based on the level of impact to your business

There is no question that foreign exchange availability, exchange rate volatility, and the resultant impact on earnings and cash flow have had a huge impact on businesses in recent times. Due to the supply chain structure in several industries, many local businesses have struggled with foreign exchange exposures. Interestingly, a few businesses are starting to consider non-traditional means such as blockchain technology either in the form of the Bitcoin digital currency or cross-currency swaps based on the blockchain to manage currency risk exposure and drive efficiency. This is in line with global trends where we are seeing a rise in corporates that are encouraging use-case testing and experimentation around blockchain. For CFOs that seek to explore this route, there are regulatory and tax considerations that must be addressed properly. This will require significant collaboration across industries, regulatory bodies and those supporting potential solutions. Whilst much of these are in the early stages, it is important to ensure robust risk management frameworks and hedging strategies - especially as we have seen recent volatility in the price of Bitcoin. This should contribute to better decision making and enhance business performance.

CFOs appear to be showing a high level of apprehension for Currency Risk and Liquidity Risk. This aligns with the lowered expectations of growth in the economy underlined by the identification of fluctuating exchange rates as one of the major sources of concern for businesses.

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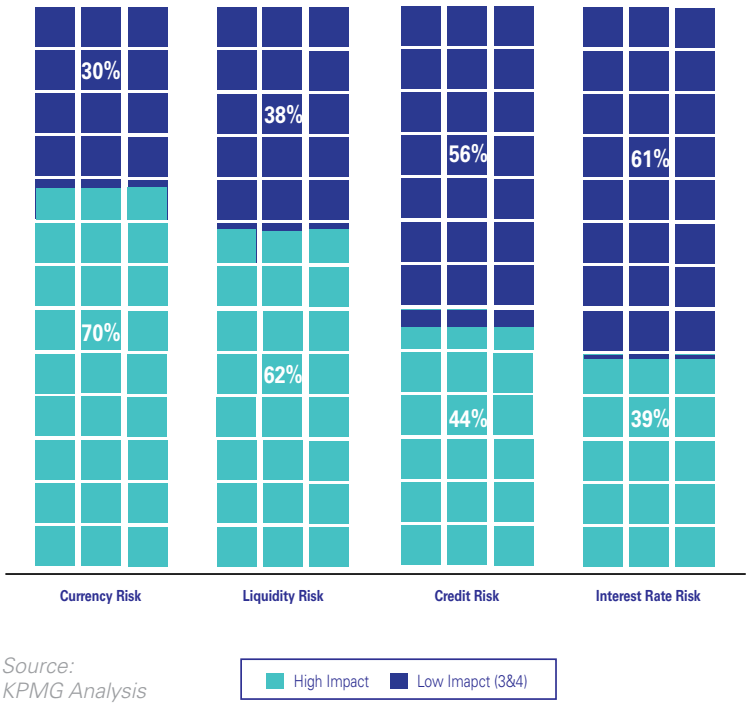


Source: KPMG Analysis

SECTION THREE

Enabling Environment

"The ease of doing business parameters shed a bright though sometimes unflattering light on regulatory aspects of the business climate in a country. Efficient business regulations are key for a blooming private sector and are important for overall development."

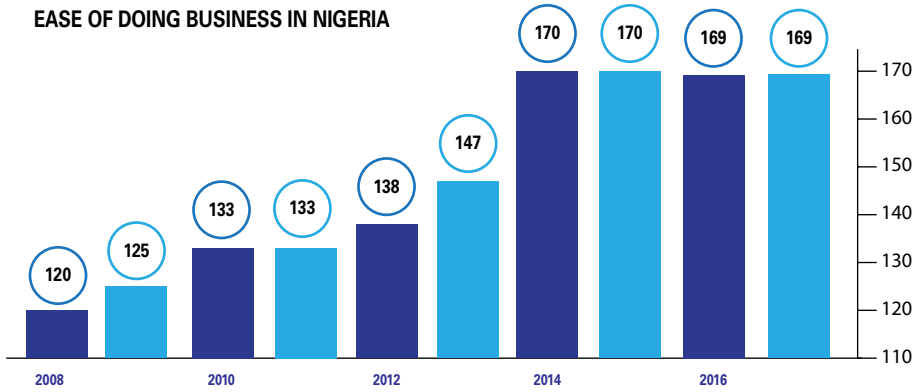
Ajibola Olomola
Partner
Tax, Regulatory & People Services
KPMG in Nigeria

Q14

KPMG INSIGHT

Doing Business provides quantitative measures of regulations for ten indicators. By gathering and analyzing comprehensive quantitative data to compare business regulation environments across economies and over time, Doing Business index encourages countries to participate towards more efficient regulation; offers quantifiable benchmarks for reform; and serves as a resource for academics, journalists, private sector researchers and others interested in the business climate of each country. As an economy achieves a better performance compared to others, it will be seen as more attractive for new investors. Good governance is predominantly essential for businesses. Transactions costs are lower when regulations are simple, transparent and predictable. Entrepreneurs do not have to waste valuable resources on red tape, thus, enabling anyone to do business without having to resort to connections or informal payments. For the World Bank Group, it demonstrates an ability to provide global knowledge, independent of resource transfer and conditionality. The annual exercise generates information that is relevant and useful. New Zealand has topped the Ease of Doing Business rankings in 2017. With sustained reforms, countries can make significant improvements in its rankings in the few years. It is important that as a country, we begin to actively seek ways to improve our ranking, lessons must be learnt from the past and achievable goals in specific areas and in a given time period must be set.

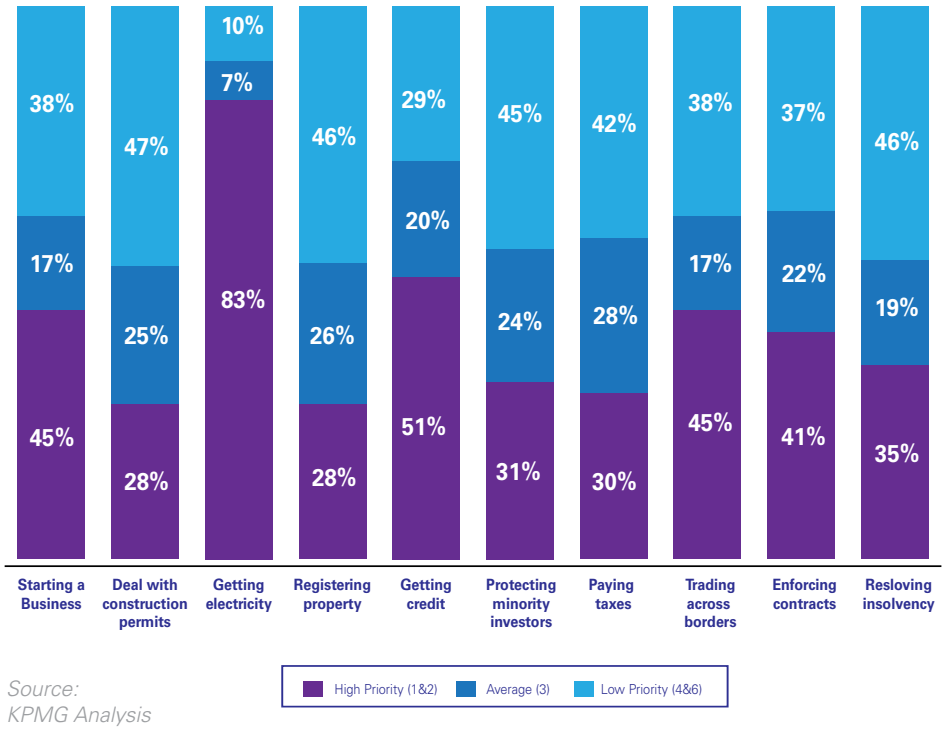
Nigeria is ranked 169 among 190 economies in the ease of doing business, according to the latest World Bank annual ratings. The rank of Nigeria improved to 169 in 2016 from 170 in 2015, but remained at the same level in 2017. Ease of Doing Business in Nigeria averaged 147 from 2008 until 2017, reaching an all time low of 170 in 2014 and a record high of 120 in 2008.



SOURCE: www.tradingeconomics .com | World Bank

According to CFOs, solving the power problem in Nigeria would be a major catalyst for any expected growth over the next few years. 83% of respondents consider the provision of reliable electricity to be a major priority for government.

Availability of Credit, Starting a Business, Trading Across Borders and Enforcing Contracts are other important priority areas that CFOs have highlighted that government should pay attention to facilitate the ease of doing business in Nigeria.



Source: KPMG Analysis

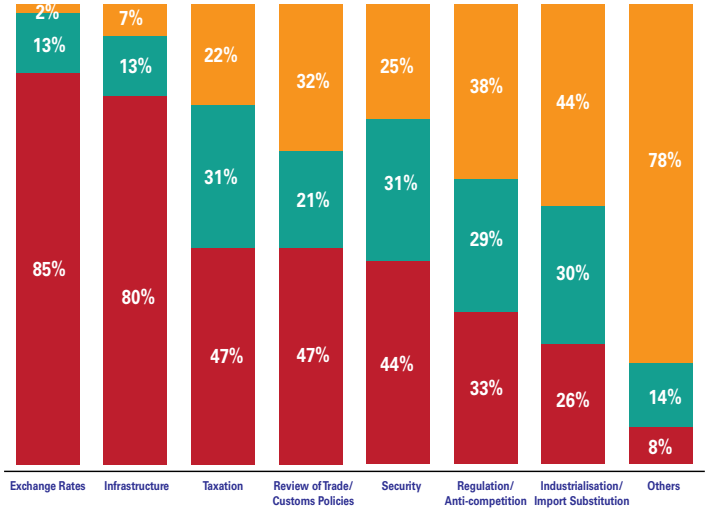
Q15 Which of the following would you rate as the highest priority area in which you would like to see improved government support for your industry/ organisation?

KPMG INSIGHT

Economic infrastructure has played a positive role in the growth performance of countries in recent times. Where development of economic infrastructures has followed a rational, well-coordinated and harmonized path, growth and development has received a big boost. Better management of economic infrastructure would have positive income and employment effects on the economy. Currency fluctuations are a natural outcome of the floating exchange rate system that is the norm for most major economies. The exchange rate of one currency versus the other is influenced by numerous fundamental and technical factors. These include relative supply and demand of the two currencies, economic performance, outlook for inflation, interest rate differentials, capital flows, technical support and resistance levels, and so on. As these factors are generally in a state of perpetual flux, currency values fluctuate from one moment to the next. Although a currency's level is largely supposed to be determined by the underlying economy, the tables are often turned, as huge movements in a currency can dictate the economy's fortunes.

An overwhelming number of respondents (85%) will like to see improved government support in terms of exchange rate policies, as a major spur for the growth prospects of their industry/ organisation.

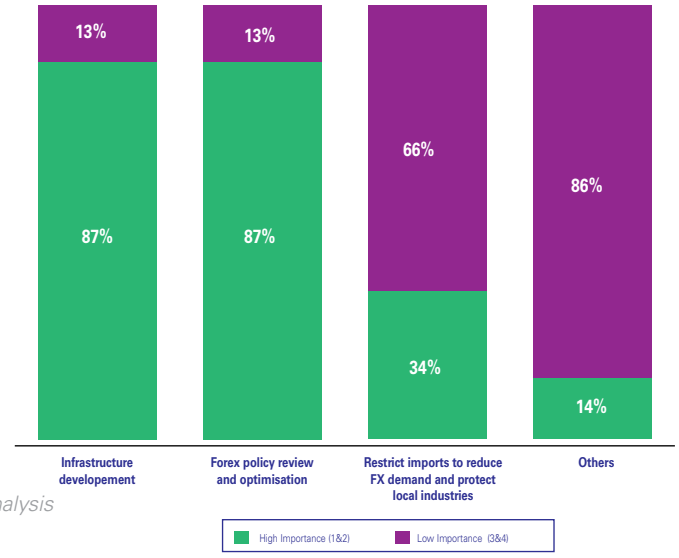
The second major area of priority for improved government support is infrastructure, as indicated by 80% of CFOs



Source: KPMG Analysis

Q16 In your opinion, which of the following options are most important in addressing the current economic challenges?

Nine out of every ten CFOs surveyed believe that infrastructure development and forex policy review/ optimization are the most important options in addressing the current economic situation in the country.



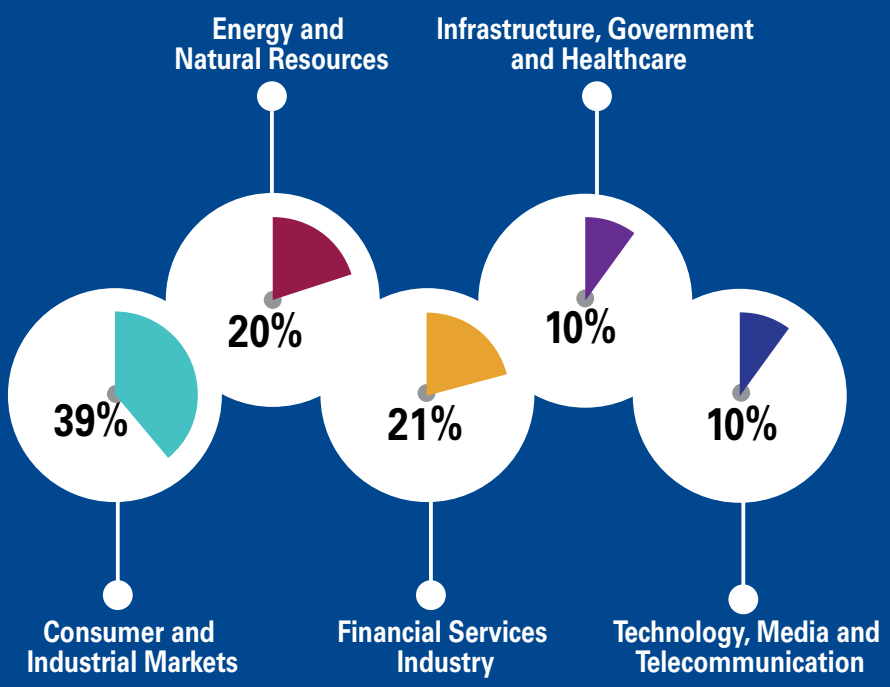
Source: KPMG Analysis

About the Survey

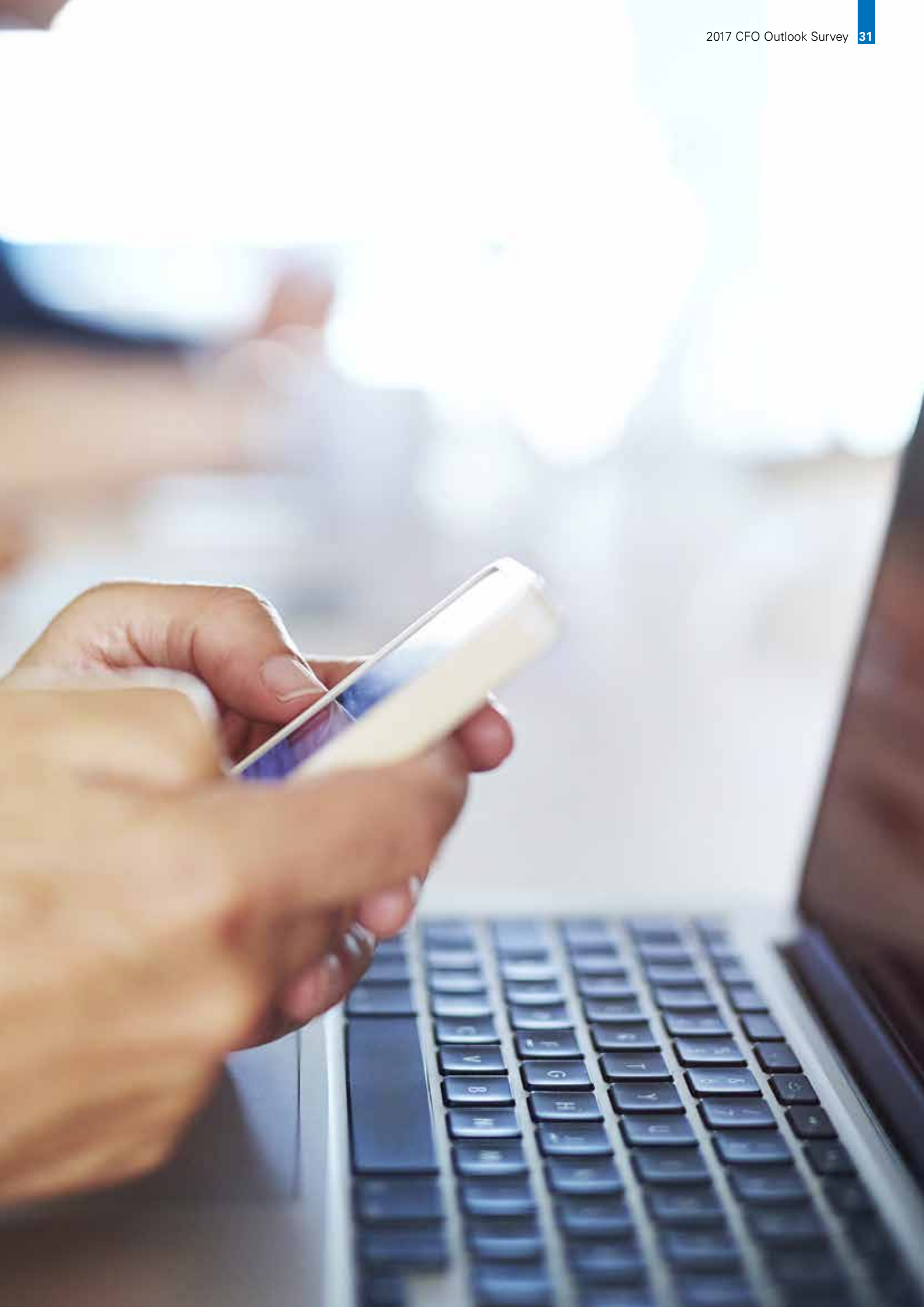
KPMG International's global survey of CFOs and other senior finance executives of organizations worldwide is one of the most comprehensive and long-running survey series of its kind. Iterations of our global CFO surveys and research papers have been conducted regularly since 2006, charting the evolution of finance departments and identifying leading financial management practices of high-performing companies.

This report presents our findings from the 2017 CFO Outlook Survey conducted by KPMG in Nigeria which consists of sixteen (16) questions. CFOs and Heads of Finance in leading organisations across all major sectors in Nigeria shared their opinions on the outlook for their businesses, their strategies for cost and risk management and the priorities for an enabling environment.

The distribution of our respondents across the sectors is illustrated below:



We also interviewed key subject-matter specialists and finance advisory leaders and drew from other KPMG International survey reports and Financial Management thought leadership in order to ensure the report also provides additional insight into some of the key themes identified in the survey.



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