Inside the mind of the investor… What's next?

554

investment professionals in 59 countries surveyed

55%

of investment professionals say globalisation has not helped to close the gap between rich and poor

68%

of investment professionals say it's harder for businesses to sustain trust

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Introduction

Investment professionals around the world are upbeat about global economic growth prospects, despite the shifting political landscape. They also told us about just how much they see the world changing because of technology.

Richard Sexton
Vice Chairman, Global Assurance

This year, we have again set out to gauge sentiment among investment professionals and compare it with the views of chief executive officers (CEOs). We asked the two groups about their opinions on growth prospects, the threats that companies face today, and the challenges and opportunities presented by technological innovation. We also sought their views on the factors that influence the trust placed in business and on the effect and future of globalisation. Their responses unsurprisingly showed a variety of perspectives.

Our CEO survey,[1] given its 20-year history, highlighted some of the changes that CEOs have experienced over that period. Our research among investment professionals hasn't been running that long, so we asked them about the big developments they have seen over their careers. They described the changes they've seen in behaviour and market dynamics, the rise of index investing, an increased focus on governance and shareholder engagement and the growing importance of environmental and social issues.

And of course they mentioned technology, particularly the proliferation of data and the need to deal with a 24-hour news cycle. Data is now produced more quickly, from more sources and disseminated more rapidly. This isn't necessarily always seen as a positive change; if done badly, it can lead to confusion, ambiguity and rushed decisions. For many respondents, the mass of data now available has become as much a challenge as a blessing.

Our research this year identified a number of areas in which companies could provide more explanation to investment professionals and other stakeholders: their approaches to support innovation, the need for a strong corporate purpose and values, steps being taken to prevent cyber-attacks and data breaches, and the benefits and costs of running a global business are a few examples. And in a world of ever-increasing amounts of data, companies should remember that, although the information they provide should of course be complete, it also needs to be relevant and not overwhelming.

I hope these findings will help to improve the quality of engagement – and perhaps understanding – between companies and the investment community. I would like to thank all the individuals who took the time to answer our surveys and speak to our researchers in person. Without hearing their opinions, we would be unable to share these insights.

Section one

Section two

Section three

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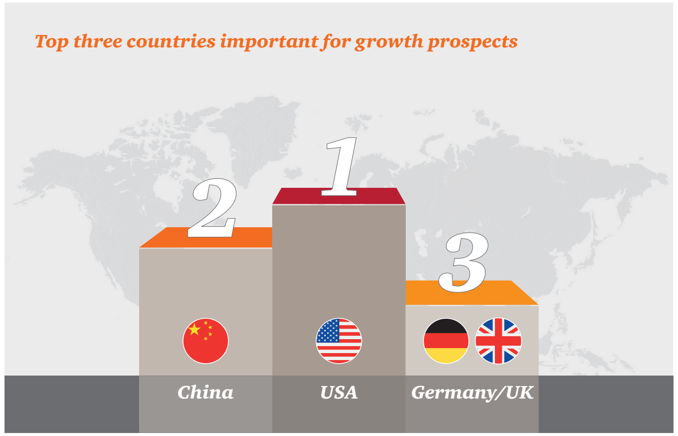
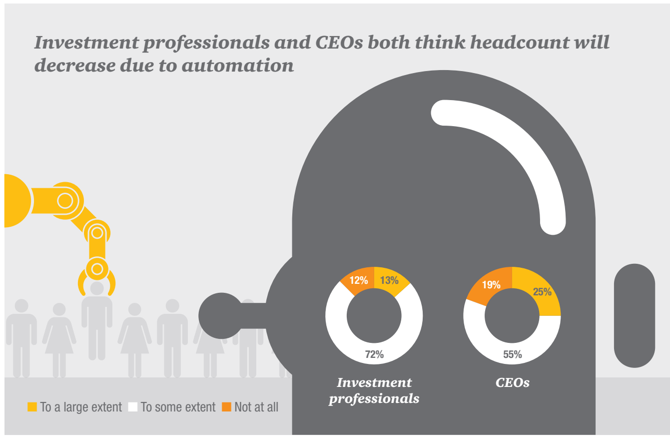
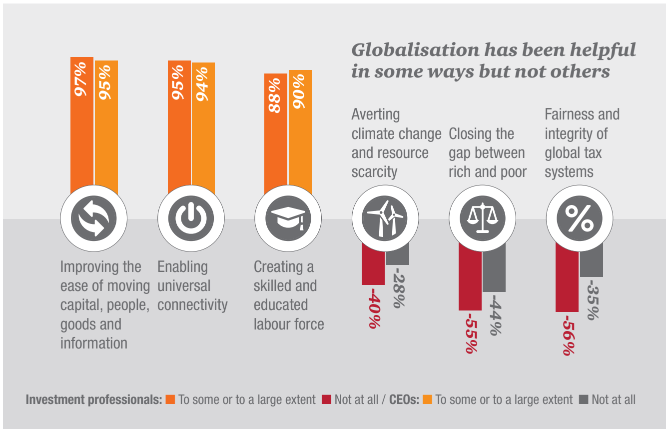
Further reading

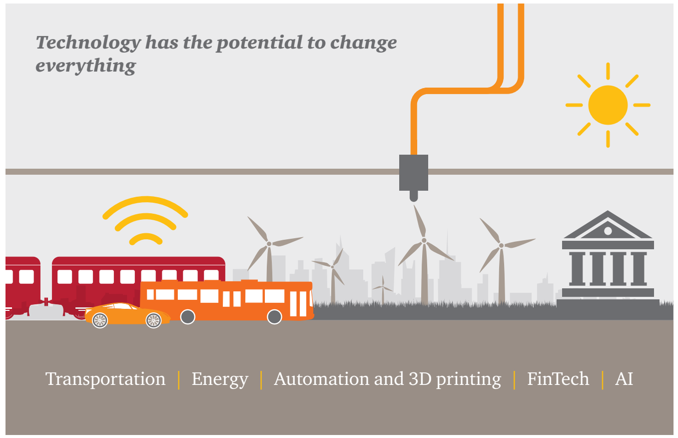
Inside the mind of the investor

Executive summary









Pursuing growth in an unpredictable political environment

"In the aggregate, we are probably going to be alright."

Despite the considerable political uncertainty across the world, our latest global survey of investment professionals found relatively high levels of optimism about global economic growth prospects. Nearly half of the 554 investors and analysts who responded to our online survey expect global economic growth prospects to improve over the next 12 months – a higher percentage than last year. They are also more optimistic than the 1,379 CEOs and analysts who responded to our online survey expect (a reversal from last year). Although our 38 qualitative interviews with investment professionals showed a wide range of opinions, modest growth is the most common expectation.

Increased confidence in global economic growth prospects has fed through into expectations for company-specific growth prospects. CEOs are particularly confident in their own company's revenue growth prospects, while investor confidence tends to vary by industry.

From a regional perspective, investment professionals see the USA as most important for the growth prospects of the companies they invest in or follow over the next 12 months. China comes second, with Germany and the UK tied in third place. The top four countries match those identified by CEOs.

We also explored their views about globalisation. Many investment professionals think it has brought benefits, for example, making it easier to move capital, people, goods and information, as well as enabling universal connectivity and creating a skilled labour force. And while they don't expect the globalisation process to stop or be reversed, they do see some negative effects of globalisation, with many having fresh memories of the global financial crisis. They also think it has not helped to close the gap between rich and poor, with some suggesting that wealth inequalities are helping to drive social unrest and moves towards protectionism and nationalism.

And investors and analysts, like CEOs, think it is becoming harder for business leaders to balance competing in an open global marketplace with trends toward closed national policies. They want companies to understand the markets they enter, act in socially responsible ways and support local economies.

Doing business in uncertain times

"Companies with good management will evolve and adapt to embrace the challenges and utilise them as opportunities."

Investment professionals acknowledge that companies face many threats, but this year, as last year, they perceive geopolitical uncertainty as the top threat to company growth prospects. Protectionism, the future of the Eurozone and social instability also rank highly. These four issues are interlinked, reflecting nationalist trends around the world, and all can affect growth through their impact on the global economy.

The investors and analysts we surveyed are also becoming increasingly concerned about cyber security. This threat leapt to joint fourth place, up from ninth in last year's survey.[2] Investment professionals expect companies to be proactive in addressing cyber risks.

The main threats to growth prospects identified by investment professionals differ noticeably from those highlighted by CEOs. Business leaders generally focus more on business-related risks, such as the availability of key skills and an increasing tax burden. In general, our interviews with investment professionals confirm their belief that talented management teams can turn threats into opportunities for their companies. Their aim is therefore to invest in companies that have those talented management teams.

Given the uncertain business environment, what one thing could companies strengthen in order to capitalise on opportunities? Investment professionals and CEOs both highlight the importance of innovation. In conversation, many investors and analysts highlighted the importance of companies being agile and able to respond to changing consumer requirements, business models and technology.

Technology as a disruptor and enabler

"From every angle, it comes back to data and technology."

Although it feels like the speed of technological change is ever faster, the investment professionals we spoke to seem to think the speed of change is slowing. They are more likely than CEOs to think industries have been transformed by technology, particularly in the technology and telecom sectors. Looking ahead, investment professionals and CEOs both expect technology to have a further significant impact on competition, particularly in the consumer services and technology industries.

Investment professionals think that numerous aspects of today's world will be fixed, disrupted or replaced by new technology. Artificial Intelligence and automation are widely expected to have an impact, alongside the introduction of autonomous vehicles, new sources of renewable energy, advances in genetic research and FinTech developments. Technological progress could also affect the globalisation trend: by making production cheaper in developed countries there will be less of a need for outsourcing to developing countries. As well as seeing benefits from increased automation, investment professionals are also concerned that it could damage the customer experience.

The vast majority of investors and analysts think companies' headcounts will decrease as a result of automation and the adoption of other technologies. Many sectors are likely to be affected. However, they also think that automation and new technology may in fact create new roles and change the skillset employees will need. As a result, companies will need to educate their employees about the changes taking place and to invest in retraining to make sure people have the skills needed for the changing workplace. They also think the government needs to work on changing the education system to ensure people learn the necessary skills from a young age.

When asked about the importance of a range of skills employees need today, investment professionals prioritise creativity and innovation, alongside adaptability and problem solving.

Maintaining trust in the digital world

"A good company will be aware of the risks involved in not addressing trust."

Concern about a lack of trust in business has increased slightly this year, among both investment professionals and CEOs. Having said that, in our interviews, some investment professionals were very clear that they think the general 'trust deficit' debate is overblown.

But trust comes in many forms and one of the challenges facing companies today is that data about them, their competitors and industries is produced from so many sources. This makes it harder for them to build a story over time and harder to ensure that what's being said about them is accurate. Our interviewees spoke about the need for companies to tell their story consistently and actively manage social media messaging.

Investment professionals also talked to us about the impact of technology on trust and the need for governance (e.g. to manage cyber security, data outages and data privacy risks). They are aware that they need to ask the right questions of companies in order to understand the technology-related risks they face.

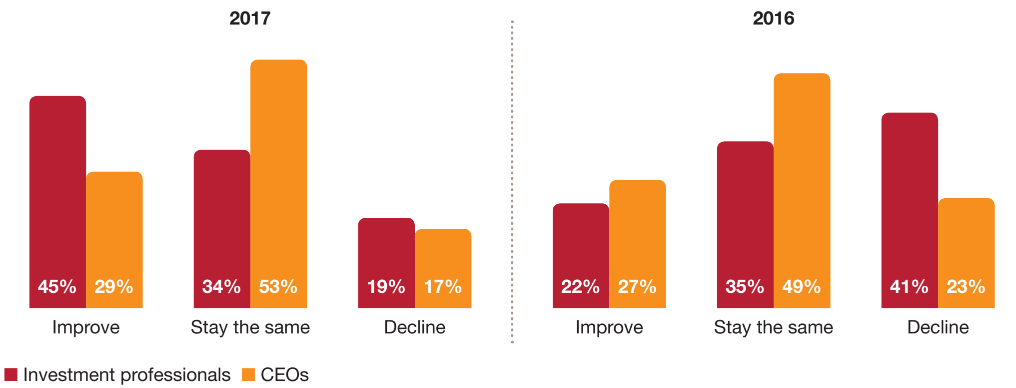
In our interviews, investment professionals acknowledged the challenge companies face in managing the expectations of different stakeholders, including shareholders, governments and employees. They think companies can meet the needs of various stakeholders simply by doing what they are in business to do – that is, focusing on the long-term success of their core business.

This year's research has emphasised yet again that companies face a huge challenge in explaining clearly how they are capitalising on opportunities, harnessing technology and addressing the many threats they face in today's world. As one investment professional told us, "The key is understanding why your messages are complex, but then trying to make them simple."

Pursuing growth in an unpredictable political environment

Figure 1: Investment professionals are more confident about the global economy this year

Q: Do you believe global economic growth will improve, stay the same or decline over the next 12 months?



"I expect modest growth, nothing spectacular. Markets are on steroids from the central banks and, for the next year, central banks will ensure that accidents that should normally happen won't happen."

"Global reflation will occur with the new US president. Interest rates will rise and an increase in public investments will enhance economic growth. Overall, the economy looks good in the short run."

The extent of political change under way in significant markets such as the USA and UK, and the possibility of future government changes in several European Union nations and even some Sub-Saharan African countries, has led to an increased sense of uncertainty across the world. Has this shaken the confidence of investment professionals? Perhaps surprisingly, our latest survey finds that for many it has not. Asked about their expectations for global economic growth, investment professionals are rather optimistic – nearly half expect global economic growth to improve in the next year. Their optimism is far higher than in last year's survey and higher than the optimism shown by CEOs (who are also more optimistic than last year, just not by as much). This more optimistic view is consistent with PwC's latest Global Economy Watch[3], which predicts a modest increase in global growth in 2017 relative to 2016. And because investment professionals were starting from a lower base, perhaps they have accelerated up the optimism scale more quickly than CEOs have.

But some of our interviewees held a less bullish view. As one interviewee said, "I think this is priced in already and the impact on the markets will be minimal." A few investment professionals told us they expect an element of reflation as governments try to curb the effects of deflation by implementing policies such as reducing taxes or changing the money supply.

"In the USA, the new president is likely to stimulate the economy with a fiscal package. It may create a euphoria and stock prices may rise for a temporary period, but it will not last long."

"Growth will be weak, bleak and unpredictable."

And although some acknowledged that there may be opportunities created by political change in the USA and UK (and indeed elsewhere), some are concerned about global growth coming from fiscal stimulus. "It could have short-term benefits even if such growth may not be sustainable in the long term," said one interviewee. Another commented: "It is precariously balanced. Political instability could determine what happens."

The strength of the economy has a bearing on a company's own growth prospects. So it's no surprise that the increased confidence in the global economy seems to be having a similar effect on investment professionals' confidence in company revenue growth potential in the short and medium terms (although in a less pronounced manner). And, like last year, CEOs are more confident than investment professionals in their own company's revenue growth prospects.

But investor confidence varies by industry, whether in the short or medium term (unlike CEOs, who tend to have similar confidence in their companies' revenue growth potential, regardless of industry). See 'Looking for more data?' section below for details.

Figure 2: Confidence in revenue growth over the next 12 months has increased from last year

Q: How confident are you about the prospects for company revenue growth over the next 12 months?

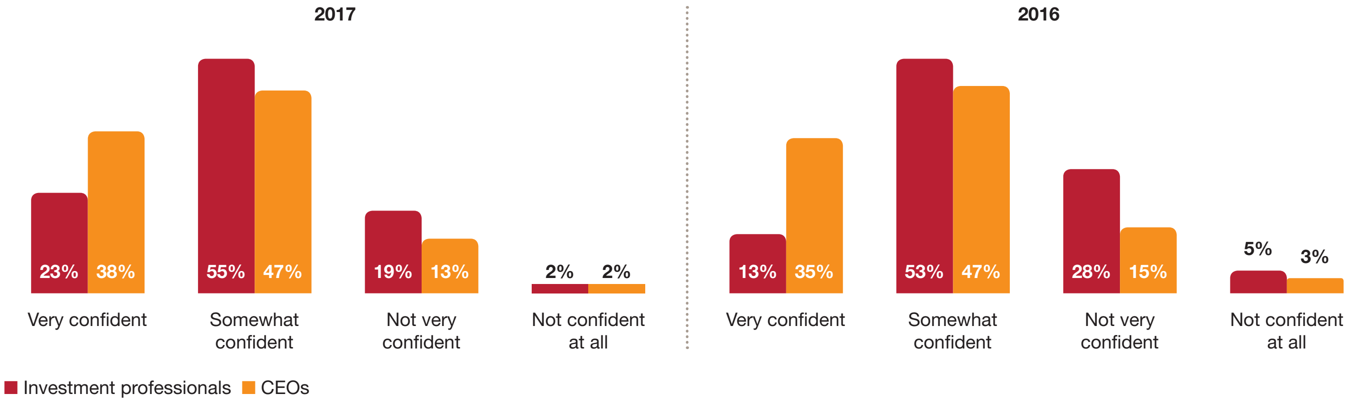


Figure 3: Confidence in revenue growth over the next three years is similar to last year

Q: How confident are you about the prospects for company revenue growth over the next three years?

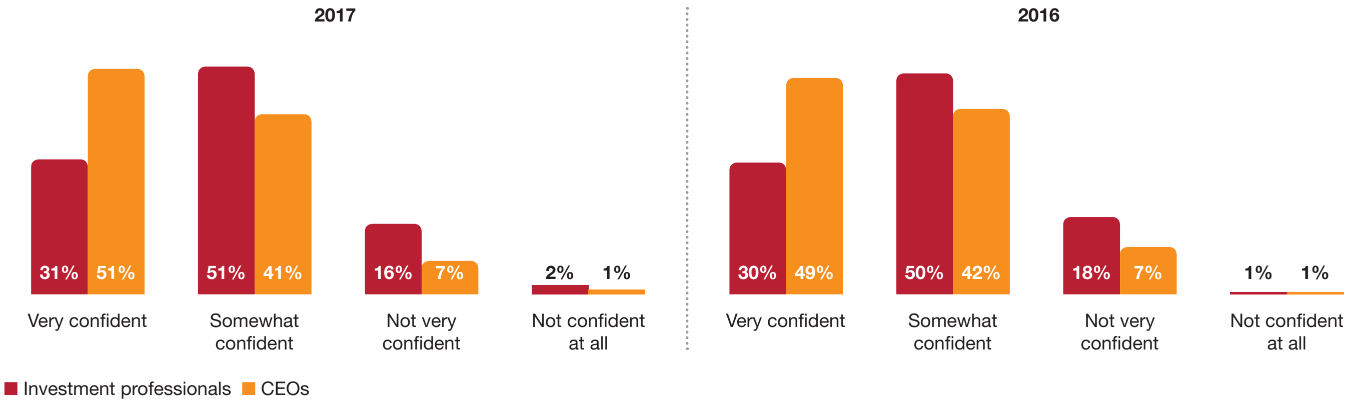


Figure 4: **Investment professionals see the USA and China as the most important countries for growth**

Q: Which three countries do you consider most important for overall company growth prospects over the next 12 months?

% of respondents naming this country in their top three

	Investment professionals	CEOs
USA	85% (2016: 89%)	43% (2016: 39%)
China	62% (2016: 71%)	33% (2016: 34%)
Germany	32% (2016: 39%)	17% (2016: 19%)
UK	32% (2016: 19%)	15% (2016: 11%)
India	10% (2016: 12%)	7% (2016: 9%)

■ Investment professionals ■ CEOs

"In the spotlight in particular will be Asia, and China and India most noticeably given their changing population landscape. It will be interesting to see how the USA plays out and the longer-term implications of Brexit, plus the 'togetherness' of the EU more generally."

"Europe could surprise, but it depends on what happens in the USA."

"The US economy, and to some extent the UK, is a 'watch and wait' area for investors."

Continued focus on the USA

With all the change happening in the world today, where will the growth come from? "Economies with fiscal dominance will grow the most, plus we'll see growth from emerging markets," one of our interviewees told us.

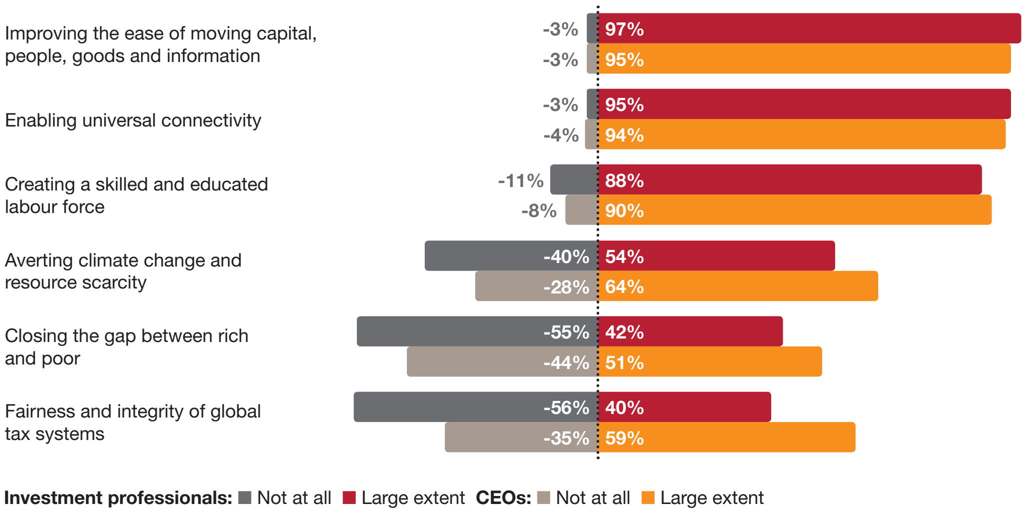
The top five countries that investment professionals consider most important for companies' overall growth prospects over the next 12 months are the same as last year. Our survey shows that the USA has retained its dominant hold on first place and China again comes in second. One interviewee said, "China is becoming more important and will continue to grow but at a slower pace."

It's striking that the UK is now seen as more important for growth, particularly by investment professionals, moving up from fourth place last year to tie in third place (with Germany) this year. Those focused on the technology and financials industries in particular put the UK among the top three countries important for growth. India retains fifth place for investment professionals but moves to sixth place, following Japan, for CEOs.

But does 'importance' equate to 'positive growth' and therefore optimism? Maybe or maybe not. Importance could be interpreted in a positive light – that the countries selected would be those expected to grow most or fastest. On that basis, the Brexit vote and all the uncertainty surrounding the UK's future relationship with the EU appear not to be deterring investors. However, some investment professionals we spoke with saw that 'importance' could also be interpreted in a negative sense – that problems and greater volatility in the UK, for example, could have an important effect on slowing down companies' growth. Our findings may well, therefore, include a mixture of positive and negative sentiment.

Figure 5: **Investment professionals see benefits and downsides to globalisation**

Q: In your view, to what extent has globalisation helped with the following areas?



Globalisation in the spotlight

In any discussion about growth prospects, the topic of globalisation inevitably comes up. There are indications that globalisation is no longer driving growth to the extent it once did. Between 1980 and 2007, global trade grew much faster than global gross domestic product (GDP); since then, it's been lagging.[4] Many reasons for this slowdown in global trade have been identified, including China's rebalancing denting demand for commodities and the increased regulation that followed the financial crisis.

The growing disillusionment of the public, with the knock-on effect that has on national government policies, is also an important factor. Recent political events seem to be revealing the extent to which voting populations feel their livelihoods and cultures are under threat from the free trade forces of globalisation. One interviewee pointed to what he calls a trilemma, based on the work of economist Dani Rodnik: choosing between (1) globalisation, (2) the nation state and (3) democracy.[5]

"Political, economic and social risks have increased. Globalisation has probably gone too far."

"Companies are looking for growth, and they can only find this when they go global."

"People are happy when goods and money change hands quickly, but when people move across borders there is a different reaction. This is a bit like a pendulum – now there is a natural push back against migration, technology, job transformation and disruption. The ability to sell the broader benefits to people has been challenging."

"CEOs and business leaders must get involved in social issues like income inequality that may be slowing down growth."

There are a variety of views about how globalisation has been helpful. For example, one interviewee said globalisation is beneficial because it has helped to improve innovation: "Low liquidity of labour causes innovation to become stale." Another pointed out that it helps companies focus on what they do best: "Let other countries make it cheaper and you should find something else to do." Some investment professionals see benefits from having local input from the markets in which companies want to do business. As one said, "Most large businesses globally have figured it out: you need that bit of local touch to do well."

However, investment professionals and CEOs are also aware of the negative effects of globalisation. They both think that globalisation has not helped in closing the gap between rich and poor. Perhaps they recognise that wealth inequalities, resulting from or exacerbated by globalisation, are significant drivers of social unrest and the political mood swinging towards protectionism and nationalism. But the concern about the gap between the rich and the poor is not new – a look through history uncovers some decades-old publications that emphasise the need for a company to remember its role in society and its obligations to a range of stakeholders (see, for example, the so-called Trueblood Report from 1973[6] and corporate finance textbooks as far back as the 1940s[7]). But there may be a positive aspect to this gap. As one interviewee said, "The gap in income is what makes innovation possible. What is important is to ensure equality of opportunities."

Climate change is another area receiving increased attention, with business and government leaders around the world working together to reduce the effect of pollutants on the environment and to address resource constraints and other risks. But climate change is not only a scientific debate, but also a political debate. So it's not surprising that CEOs express more disagreement than investment professionals that globalisation has helped make progress in this area.

We also asked our interviewees about the role of business in solving societal problems, whether a result of globalisation or otherwise. Many of them think that responsibility lies with government, although one said, "If governments can't make change, businesses should take it on themselves to do something." Another said, "You need private sector capital while the government creates the enabling environment."

Looking for solutions

The investment professionals we talked to certainly don't think globalisation is over or that it can even be substantially reversed. Turning the clock back is impossible. As one investment professional put it, "Now that globalisation is out of the box, you can't put it back in." Another noted that pulling back on globalisation would be costly for companies and would increase prices for consumers: "Developing countries will be the biggest losers in this, and things will be more expensive in the local country."

Companies need to find a way to continue benefiting from globalisation, while also responding and adjusting to a new world order that could bring higher trade barriers, tighter restrictions on labour movement and protectionist policies designed to support local companies. The investment professionals we spoke with emphasised the need for companies to 'understand the market they're going into' and 'be a socially responsible company in the country in which they want to operate.'

Asked what CEOs could be doing to achieve a balance, one investment professional encouraged companies to support local economies on the grounds that "local value leads to global value, but not necessarily vice versa." Another talked about our raised awareness of where what we buy comes from: "Companies need to think about how they distribute their products. We're all more aware of what we buy, wear, etc. Our decisions impact other people and we need to understand the supply chain." To make globalisation more palatable, our respondents suggested that companies should 'educate themselves, their employees and policy makers', 'be transparent, honest and open' and 'make an effort to build trust with and listen to stakeholders.'

"In a globally-connected economy with the internet, unless extreme ideology gains power or regulation becomes unreasonable, a setback in globalisation will be limited and there should be a point where it settles."

Tough questions about pursuing growth in an unpredictable political environment:

1. Are you explaining clearly enough how the global economic environment may affect your company in particular and the industry more generally?
2. Are you telling your growth story, and the reasons for your outlook, as effectively and understandably as you could be?
3. As the impact of globalisation is increasingly debated, are you talking to your stakeholders about the benefits and challenges globalisation brings to your business and local communities?

Doing business in uncertain times

"Geopolitical uncertainty still remains the biggest risk that companies face. Everyone is affected by these risks."

"Political trends have all of a sudden become more important. It's a new trend, a new experience, which has to do with inequality."

"There are more threats and uncertainties due to the political uncertainty around the globe; for example, with Brexit and lots of populist movements in Europe. But I don't think the economic situation is as bad as it was during the financial crisis."

In addition to the uncertainty companies are facing about the future of globalisation, there seems to be no shortage of threats facing companies, whether political, social, environmental or just simply from being in business today. "I would have answered that there are more threats each year for the past 15 years, which of course isn't right," said one of our interviewees.

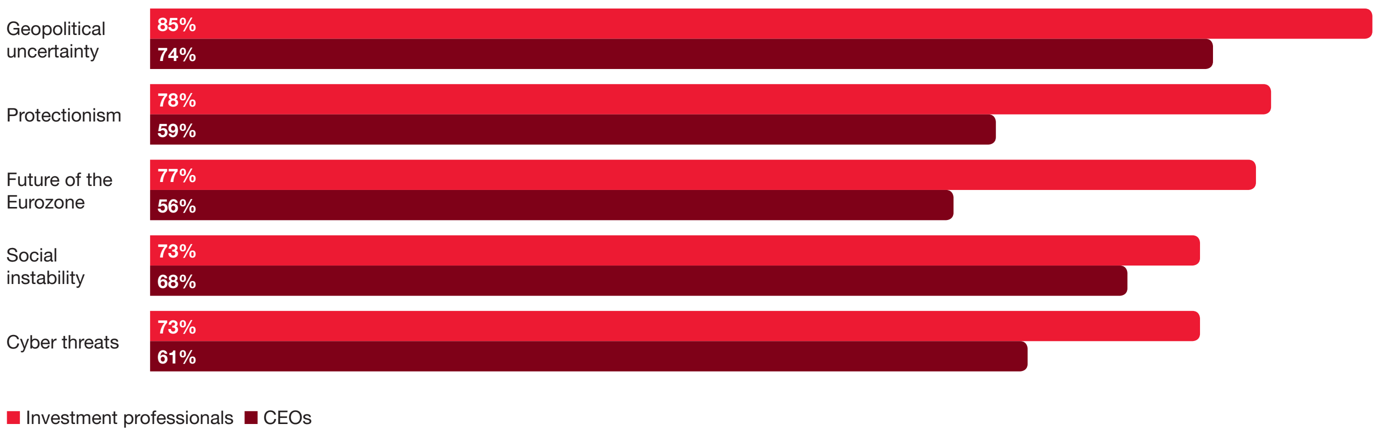
There have always been multiple threats to growth, and there always will be. But which threats are causing most anxiety at the moment?

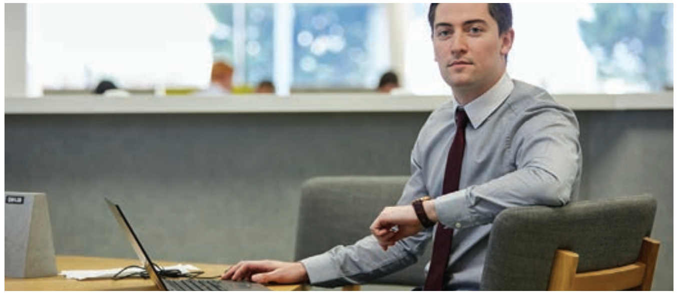
Geopolitical uncertainty is seen as the top threat to company growth prospects, as it was last year, but concern has grown. Protectionism, the future of the Eurozone and social instability follow close behind, reflecting recent and

Figure 6: Investment professionals see geopolitical uncertainty as the top threat to growth

Q: How concerned are you about potential economic, policy, social, environmental and business threats to company growth prospects?

% of respondents answering somewhat concerned or extremely concerned





forthcoming political events (such as the US election and UK Brexit vote). These four issues are interlinked, and all can affect growth through their effect on the global economy.

The potential effect of protectionist policies came up regularly in our interviews with investment professionals, some of whom doubt whether such policies can have as positive an effect as some politicians and voters may think. “Protectionism may save a few jobs but companies will need to raise prices,” one told us. “Income goes up but the cost of living goes up more.” However, some investment professionals think the effect of protectionist policies may be overplayed. As one said, “There are a lot of automation projects happening that could have a bigger impact. These issues are a tad exaggerated.”

Cyber security is a growing concern for investment professionals, moving to joint fourth place from ninth last year. This is possibly exacerbated by high profile government and corporate hacking incidents. More than one investment professional told us, “Cybersecurity is the main issue on people’s minds, across industries.” Our survey results highlight that investment professionals and CEOs in the financial services and technology industries are particularly concerned about cyber threats.

“There are not necessarily more threats now, just different threats. Companies are always faced with challenges. I am impressed with the flexibility and management skills of companies to address challenges. They will find a way to be nimble and creative.”

Moreover, cyber security breaches and data privacy breaches top the list of events or developments that could negatively affect stakeholder trust levels in the industry both today and over the next five years. We discuss the issue of trust later in this report.

As one interviewee said, “Hacking will be seen differently. Not as a threat, but as a normal part of doing business. You’ll know that there will be someone trying to get information from you. This is not just security, you need to determine what’s public and what’s private.” Investment professionals expect companies to be on the front foot when addressing cyber risks. One told us, “Companies have learned from breaches, but there is a lot of work to do. They must be proactive, not reactive. No business or government is immune.” Another commented that “the cyber security issue is massive,” and thought companies should face financial consequences if they fail to address it. However, he acknowledged that CEOs may be deterred from saying too much about their cyber protection strategies because “companies have everything to lose and not a lot to win by discussing cyber publicly.” But it may become mandatory for them to speak about it. The US Securities and Exchange Commission (SEC) is thinking about whether public companies should have a duty to disclose breaches.[8]

Different perceptions about threats

The primary threats to growth prospects identified by investment professionals differ markedly from those prioritised by CEOs. CEOs tend to focus more on specific, business-related risks. Investment professionals are more focused on the big picture threats, which is understandable given the effect on global wealth that significant political and economic events can have on their portfolios.

Our survey shows, for example, that CEOs are much more concerned than investment professionals about the availability of key skills, which ranks third for CEOs but doesn't even make investors' top 10. See 'Looking for more data?' section for more details.

It is also notable that CEOs are more concerned about the speed of technological change than investment professionals are, although this differs by industry. For example, CEOs and investment professionals in the financials industry are aligned in their level of concern, but CEOs in the telecom industry show more concern than investment professionals following it do. Some investment professionals we interviewed said they didn't have an issue with the speed of technological change affecting companies today, but rather with the amount of data made available and the speed of its dissemination, an issue we touch on elsewhere in this report.

The biggest divergence between the views of investment professionals and CEOs arises with the perceived threat of an increasing tax burden: investors and analysts are much less concerned about this than CEOs are. Interestingly, investment professionals are less concerned than they were about this last year (2017: 43%, 2016: 57%). They may assume that companies have strategies in place to react to any proposed increase in the tax burden, while CEOs face the reality of increased government and public focus on the cash tax contributions they make.

Capitalising on opportunities

A surprising number of interviewees think too much is being made of the threats facing business today. As one said, "Businesses are quite adaptable." Another said, "There is a tendency now that risks are emphasised more than the opportunities. In a world of uncertainty, it is crucial that companies can come up with a unique idea to survive."

Our interviews, both this year and last, also indicate a strong belief that talented management teams can turn threats into opportunities and make them work to their company's advantage. Therefore, the aim is to invest in companies that contain those talented management teams – ones who understand how to capitalise on opportunities, however they arise.

Given the current business environment, it comes as no surprise that, when asked to identify the one thing companies need to strengthen in order to capitalise on new opportunities, investment professionals and CEOs both prioritise innovation. And some of our interviewees pointed out that agility and the ability to evolve and innovate aren't just important for growth, but also for survival. For example, one described the way FinTech is changing the consumer finance business: "Financial institutions that cannot catch the trend may disappear." However, another thought the concept of agility was overemphasised, saying: "Even today, getting decisions right in terms of what the product offering is, how to make it available to customers at the right price point, is still far more important than saying 'we are agile'."

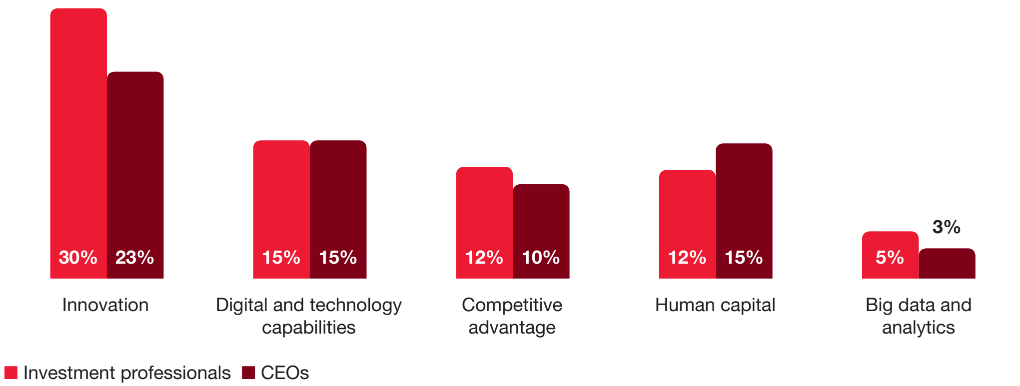
"Those who innovate will be winning all the way."

"Business models will change and some roles will be automated, but the change will take longer than people might expect. For example, self-driving cars might come but they will come slowly and gradually and, on top of that, not everybody will want to buy self-driving cars."

"Companies that innovate processes will do better; companies that innovate products always risk losing their edge."

Figure 7: Investment professionals prioritise innovation to capitalise on opportunities

Q: Given the current business environment, which one of the following do you think companies should strengthen in order to capitalise on new opportunities?



"Companies can succeed in a changing world the same way they always have – by being strategic, agile, making sound business decisions, listening and responding to consumers and the community."

"Companies should focus on the customer experience, not just making money, then they will prosper. Build relations and trust with customers and treat customers the way you'd want to be treated."

Digital and technology capabilities are also considered important by investment professionals and CEOs, reflecting the concerns held about the speed of technological change – companies will need to be able to keep up with changes in technology and identify how they can use these changes to their advantage. As one interviewee said, "Technology speaks to two things – it either enables growth or enables efficiency. Understanding technology can be a competitive advantage. It can save cost, and it can be a reason to invest today to save tomorrow." Another said, "Technology ultimately leads to efficiencies, which is better for the consumer as it stimulates competition and innovation."

CEOs place a greater importance on customer experience than investment professionals do, perhaps due to greater worry about changing consumer behaviour and the threat of new market entrants that could steal customers away. But our interviewees highlighted time and again the importance of customers to the success of a business. Many said they worry that CEOs have lost touch with customers: "The most successful companies are focused on providing value to their customers," said one. "Companies should deliver what the customers want and make the customer experience as cost effective as possible. Most companies don't do this well," said another. We also know from last year's survey that investment professionals and CEOs both see customers as the most important stakeholder group for shaping a company's strategy.

And although CEOs are more likely than investment professionals to emphasise the importance of human capital, our interviews showed that investors and analysts are indeed concerned about how technology will disrupt the workplace and potentially displace jobs. As one interviewee told us, "Automation is picking up steam. Automation will increase earnings, but will create social pressures due to people losing jobs, which may further decrease the middle class, increase political tensions and instability." One interviewee suggested that companies should educate their workforce about the forces that are triggering job losses – for example, that technology is the cause, not immigrants 'stealing' their jobs. We will explore this in the next section.

Tough questions about doing business in uncertain times:

1. Are you talking to your stakeholders about how you are addressing the opportunities and threats coming from geopolitical changes?
2. Have you told your stakeholders how you manage cyber security, data protection and privacy risks?
3. Are you explaining how you are working to ensure your business is agile enough to benefit from – and not be hurt by – disruption?
4. Given the importance of your employees to the success of your business, are you explaining the value they bring and how you monitor and maintain that value?

Technology as a disruptor and enabler

"From every angle, it comes back to data and technology."

"Growth will come from disruptive technology like electric vehicles, renewables and low carbon infrastructure."

"What will be disrupted? Everything."

Investment professionals are in no doubt about the effect technology has had on competition in the industries they follow – there are very few who think it has had no effect at all. But although it feels like the speed of technological change is increasing all the time, investment professionals have seen more change over the past 20 years than over the past five, a sign that they see it slowing.

Investment professionals have seen more radical change than CEOs have, particularly when looking at the results by industry. More than two-thirds of the investment professionals following the technology industry agree that technology has completely reshaped competition in their industry, and almost half of the investment professionals focused on the telecom industry agree with this statement. This is perhaps due to the increased popularity of and the continuous technological improvements made to mobile phones, which have an impact on both industries.

Looking forward, investment professionals and CEOs both see the next five years having at least a significant impact on competition, especially in the consumer services and technology industries. Not all potential areas of change are obvious (for example, identifying which manufacturing jobs can be done by robots). Some require 'vision' to survive, as one interviewee explained: "Companies need to be flexible to change their vision more frequently or they need to dominate the market. Most executives do not have the capability to create such a vision. They need to be responsible and proactive to be able to adapt to changes."

But technology is not seen by all as a panacea: "Computers do not get tired or make mistakes, but they cannot be as creative as human beings," one interviewee said.

Another interviewee wondered whether the vision that CEOs and chief technology officers may have for their own companies in terms of the transformative power of technology was realised in practice because he's observed that people at the sharp end – line managers – often see things differently. He said: "There is a gap between what senior leaders want a business to look like, what they think it looks like and what it actually is from an 'on the ground perspective'."

Investment professionals expect numerous aspects of today's world to be fixed, disrupted or replaced by new technology. "Technology is having a big impact everywhere; the issue is knowing which ones will take off," one interviewee said. They frequently mentioned the effect of Artificial Intelligence and automation, along with the introduction of autonomous vehicles, new sources of renewable energy, advances in genetic research and developments in FinTech.

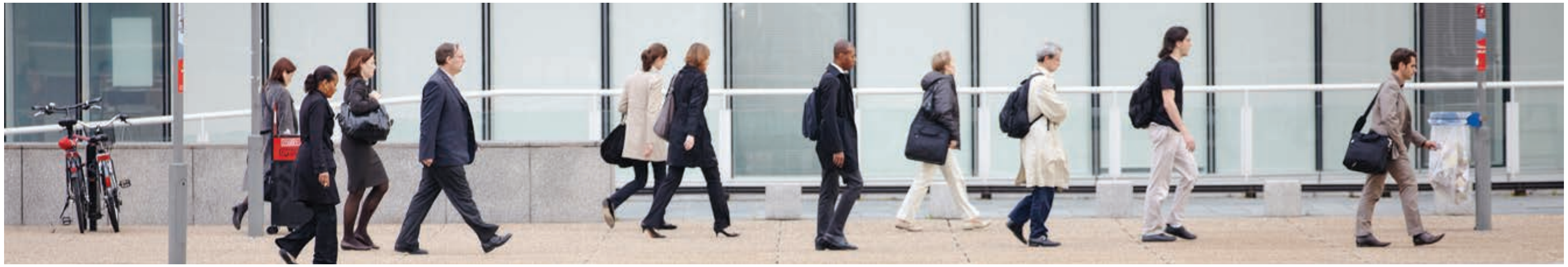
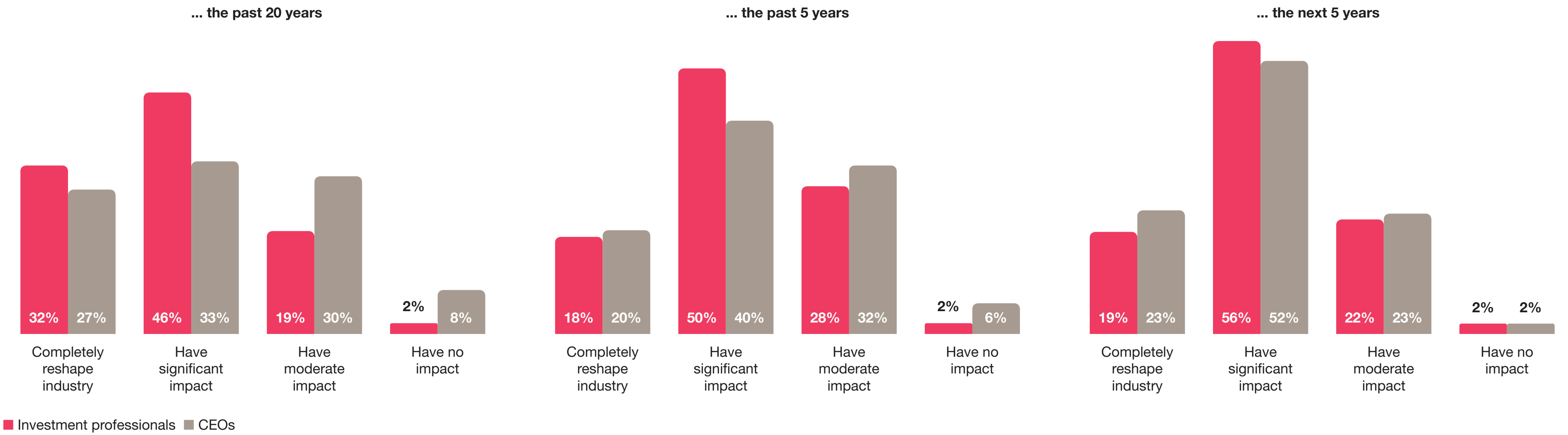


Figure 8: Investment professionals expect technology to continue to impact competition

Q: To what extent has technology changed/will change competition in the industry over …?



Not just a numbers game

One way that technology revolutionises industries is by changing the way people work – the jobs they do and the number of people needed to do them. This may explain why the vast majority of investment professionals think companies' headcount will decrease as a result of automation and other technologies (and we see this across geographies and industries). As one interviewee said, "We will see so much more automation. Automation will eliminate a lot of positions. Industry will grow, but jobs will decrease." Another commented, "Automation and digitisation are affecting white collar jobs now. Companies that anticipate it and get in early will do the best." But there is another angle to this: "You don't get flexibility with a highly automated plant."

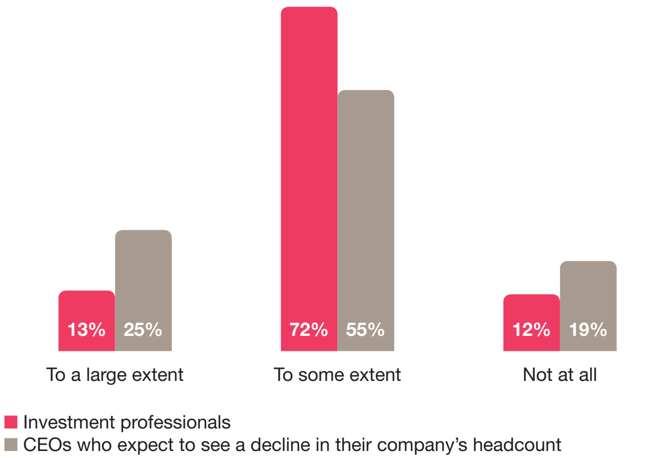
"Technology is a major catalyst for changing the workplace. When taking a one-year view, people generally overestimate the impact of the change, but taking a 10-year view, they definitely underestimate the impact of the change."

"It's too soon to know if automation will change employment significantly."

"Some companies are doing well in focusing on the collaboration between human and machine, which I think is the most powerful."

Figure 9: Investment professionals think automation will reduce headcount

Q: To what extent do you think headcount will decrease as a result of automation and other technologies?



"Automation is gaining ground even in countries where there is abundant labour at a cheap price. Some very clever people are putting their time and energy into doing something you never could have thought that a computer could do."

"New technology reshuffles employment, not lowers employment. More people are employed in companies today than ever before."

"Artificial Intelligence is emerging as the next frontier. Technology will mean that we all do different things, but it won't be the big job extinguisher that some people fear it will be. New jobs will emerge as sophisticated technology becomes more commonplace. Technology is a great democratiser so it brings with it new opportunities for others."

Mounting research and opinion validates investment professionals' expectations of falling headcounts due to technology and automation. Research by McKinsey, for example, has indicated that about 60% of all occupations could see 30% or more of their activities automated – just with technologies available today. It isn't only manufacturing and food service work that's likely to be affected, but also the financial sector, where McKinsey estimates the potential already exists to automate activities taking up 43% of its workers' time.[9] Similarly, others have indicated that thousands of jobs created in recent years to meet regulatory compliance needs in the financial sector could be replaced by automated systems.[10]

However, they may be misreading the potential effect of technological advances. As one interviewee said, "Technology on its own doesn't do anything. It is overseen by humans. It is a tool, not a driver." Some recent research has suggested that while we may see increased automation and falling headcounts in some areas, new jobs will also be created – particularly in disciplines such as IT and human resources and in frontline or customer-facing roles.[11]

And so total headcounts may not in fact decline, although employers will need to invest in developing their employees' skills so that they can adapt to the changing nature of many roles and make best use of the potential for enhanced performance offered by automation, robotics and Artificial Intelligence. "It will not necessarily be a matter of making roles redundant, but rather shifting the headcount to more value-adding areas," one interviewee told us.

Companies' actions are of course limited by employment regulations and the power of labour unions, which may vary across the world. But if headcounts are going to fall due to automation, companies will need to manage the costs of redundancies and governments will need policy measures to address the social consequences. Warren Buffett's 2015 letter to shareholders also notes the challenges and the need for "a variety of safety nets aimed at providing a decent life for those who are willing to work but find their specific talents judged of small value because of market forces."[12] One interviewee said, "A new industry or market may need to be created to absorb such people."

Another interviewee thought the lower cost of operations enabled by automation would reduce the need for outsourcing offshore. But repatriation of jobs to the home country won't necessarily result in an increase in domestic employment, despite the ambitions of protectionist policies. Automation will do what manual labour once did. "Some of the gains you had by outsourcing will be less prominent," one interviewee said. Job retraining and education would need to be part of this process. "It may cost money, but you need to think about the welfare of people," said one interviewee. Another suggested that the education system needs to change to ensure that people have the skills necessary to work in today's technology-driven world: "Even car mechanics need to know how to work with technology now."

"Businesses will use technology to continue to adapt, improve and disrupt their own business and industry. There will be more outsourcing, call centres and Artificial Intelligence."

"3D printing, if it continues to develop rapidly, can have a massive impact on the manufacturing world."

"Companies need to explain their reasoning for cost cutting to win over the local community. They also need to show respect for the people they fire."

But our interviews showed that, while automation does bring benefits such as lower-cost production, there can also be downsides and it can only go so far ("The cost savings have to stop somewhere," one said). Some investors and analysts have concerns about automation reducing the quality of the customer experience. Automated phone systems, for example, can be time-consuming to use and make it seem impossible to speak to a real person, with a potentially damaging effect on relationships. One interviewee said that the "change is so fast, everyone is overwhelmed. There are more people who cannot adjust compared to those who can."

Optimising the skills mix

While unskilled and transactional work may be increasingly automated and replaced by developments in Artificial Intelligence, people will still be needed to provide insight, make creative leaps and add the essential human touch to business activities. Finding and retaining the right talent mix remains vitally important for companies if they are to thrive, and investment professionals recognise this.

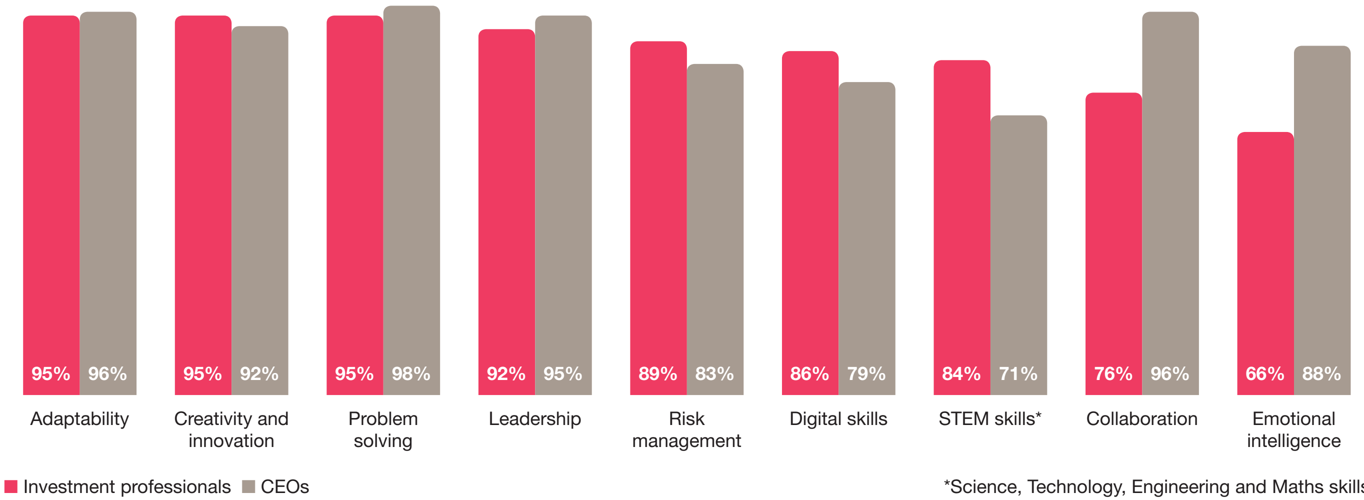
It's no surprise that, with their focus on innovation as a crucial component of capitalising on opportunities, investment professionals and CEOs agree that creativity is an important skill. Last year, investment professionals told us they wanted companies to do more to measure and communicate what they're doing around innovation. This is still an important message for companies to consider, whether explaining their strategies around their products or their people.

CEOs value collaboration and emotional intelligence far more highly than investment professionals. But some investment professionals do highlight the value of collaboration and think relationships will always be important to doing business. As one interviewee said, "Technology can never replace a physical meeting. Personal meetings are important." Collaborative skills are also valuable when working in partnership with suppliers, outsourcing service providers, governments and others. Investment professionals perhaps assume that collaboration is a natural part of corporate life. With technology, "organisational structures will become flatter, smaller, more collaborative," said one interviewee.

Figure 10: Investment professionals expect companies to have a mix of skills

Q: In addition to technical business expertise, how important do you think the following skills are to companies?

% of respondents answering somewhat important or very important



*Science, Technology, Engineering and Maths skills

"It may vary among industries, but simple tasks should shift to technology as much as possible and human beings should focus more on creative thinking. This trend is inevitable."

Investment professionals are also noticing how technology is changing the working environment, either in their firms or in the companies they invest in or follow, and they think companies need to change with it. "Successful companies must have a meritocracy. It must be all about merit – not gender or race – and we must take bias out of the equation," said one interviewee. Another thinks that "workplaces will be more flexible, roles will be less traditional and new jobs will be created. Structures are less hierarchical than before."

Tough questions about managing technology as a disruptor and enabler:

1. Are you explaining to your stakeholders how your business model might be affected as a result of new technologies?
2. Given the changing types of skills needed for companies to remain competitive, are you educating and training your employees to ensure they have the right skillset?
3. Do your employees feel they work in an environment that allows them to be creative and innovative?
4. Are you investing sufficiently in technology for the long-term success of your business?

Maintaining trust in a digital world

"All companies (and governments) need to make more effort around trust. Companies need to understand what people are concerned about, acknowledge the fact and then tell their story in a very readable, understandable way. The key is understanding why your messages are complex, but then trying to make them simple."

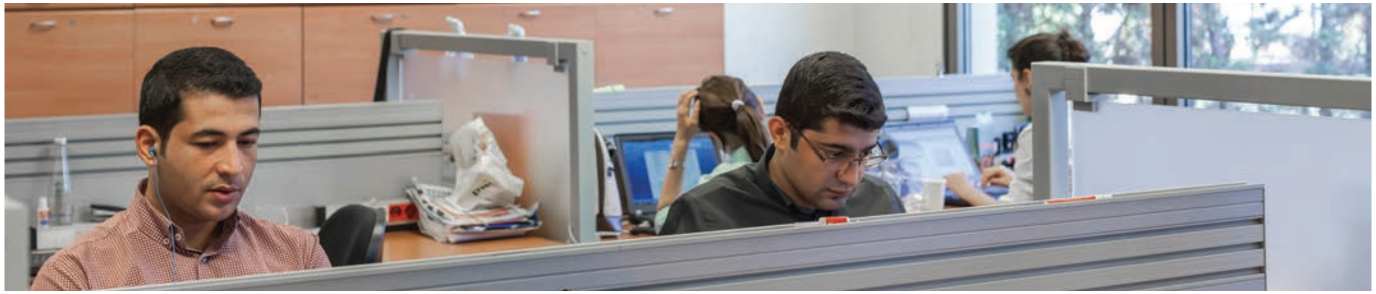
"The abundance of information made available through the use of technology has brought more transparency but also confusion and misrepresentation. The added information is not all necessarily useful. A lot of confusion and ambiguity has crept in because there is so much information coming from a myriad of sources."

Concern about a lack of trust in business has increased this year among investment professionals and CEOs, and over two-thirds of both groups agree that it's become harder for companies to gain and keep trust. But it's worth noting that there are a number of investors and analysts who don't necessarily think there is a trust deficit that companies need to address. One investment professional we interviewed suggested that people could be creating a problem where one doesn't really exist.

"Trust is binary and it's hard to measure a 'trust deficit'," another interviewee told us. "Does a trust deficit matter if a company is successful? Companies can stay in business even if they are doing horrible things, so if a company is making money and its customers are happy, is there a trust deficit?" But we think it's worth examining the qualities or actions that could either strengthen or damage public perception of a company, particularly in the context of our increasingly digitised world.

To maintain the trust of stakeholders, companies need to consider that data about them, their industries, competitors and the issues they all face is now being produced from so many sources. As one investment professional highlighted, companies used to be able to build a story over time, but they no longer have that luxury. People need to be engaged earlier. Companies need to make fuller disclosure and be prepared for users of their information to cross-check what they say, while also filling in any information gaps from other data sources or even by drawing on their own personal perceptions. "One of the things technology does is provide information to people very quickly and very democratically," one of our interviewees said. "There is no longer any place to hide. Businesses have to be mindful of how they deliver a message because fact checking is easy and quick now and you don't need a journalism degree to do it."

All this data is leading to information overload, which was a consistent theme in our interviews. One of the biggest changes investment professionals are facing is "dealing with all the information coming at you, and too much information sometimes disguises the important information." One interviewee talked about how having too much data can lead people to think that they have to make a decision, even when they don't actually have full information on an issue: "The old builders' rule used to apply in investment-making decisions – measure twice, cut once – but not anymore. Rarely do investors and analysts get the chance to measure twice."



The relationship between technology and trust came up frequently in our conversations with investment professionals. Some think it's an easy – and misguided – option to blame developments in technology for an erosion of trust. "Technology has not taken away trust in institutions, it is people who apply it," one interviewee said.

Societal and environmental issues also play a role in building – or destroying – trust. Technology is enabling greater awareness of both issues and how management teams are dealing with them. But there is some cynicism among the investment community about how companies are managing environmental and social issues. As one interviewee said, "Companies won't see social issues as their responsibility to address as long as they aren't incentivised to do so." Another thinks companies are not good at balancing the tension between cutting costs and making investments because "CEOs and management are evaluated based on profitability – and social responsibility and public relationships require costs."

Some investment professionals are more comfortable with the idea that there will always be a tension between short and long-term returns, between narrowing and expansive business activity. One told us, "The tension to cut costs, innovate, deal with social issues, etc., is not a conflict, it's life. These are not opposing needs; it is a balancing act between the short and long term."

Figure 11: Investment professionals think strong corporate purpose is vital – as well as excellent management of people's data

Q: In the context of an increasingly digitised world, to what extent do you agree with the following statements?

"Investors are mainly interested in financial information about a company. But they are showing more interest in governance now that they can actually see some relationship between short-term performance and the governance of a company. The time horizon for corporate social responsibility is much longer, so investors may not be able to see a clear correlation. But if a company has no interest in, for example, diversity, there will be some negative financial impact, so corporate social responsibility is one of the criteria for investment and companies cannot ignore this."

"Companies that are good at dealing with environmental, social and governance matters aren't necessarily good investments, but companies that are bad at it are often considered riskier investments."

"The number one priority for business is to create sustainable shareholder value."

The stakeholder expectation challenge

One of the biggest challenges for companies is to manage stakeholder expectations. The majority of CEOs agree it is important that companies are run in a way that does so (consistent with last year's CEO survey, in which 84% of CEOs thought they were expected to address wider stakeholder needs). One investment professional we interviewed sees the challenge clearly: "Shareholders want financial returns, employees in each country want jobs, governments want jobs and GDP growth, and businesses need cost-effective supply chains. There are a lot of stakeholders that businesses have to keep happy – getting the balance right is tricky." Another also emphasised the need for balance, saying: "As investors we look to try to ensure that the balance [addressing stakeholder needs] is fair; we want capital to be spent in areas where value doesn't get destroyed. It's the job of management to allocate capital sensibly."

We also sensed evidence of an expectation gap, with some investment professionals wanting companies to focus simply on running the business, regardless of the fact that CEOs feel pressured to follow a stakeholder-inclusive approach. One investment professional we interviewed said, "Emphasising the concept of multiple stakeholders won't solve the issue. Companies need to generate sustainable profits. They need to create value with their core business, otherwise their business will not be sustainable and investors will not be interested in it. Corporate social responsibility is something necessary as a means of creating profit in the long run."

Investment professionals and CEOs – but particularly CEOs – think it is now more important for a company to have a strong corporate purpose that is reflected in its values, culture and behaviours. The greater emphasis placed on this by CEOs is striking – perhaps CEOs need to explain their thinking more clearly so that investment professionals' views become more closely aligned.

"Some people think business should solve all problems. But you don't need to build a school in a local community unless it will provide, for example, a future workforce or education of people you can sell products to. Companies are not charities."

"For-profit companies need to have for-profit goals. Those for-profit goals must be broadened; companies must think about their environment broader than just their business."

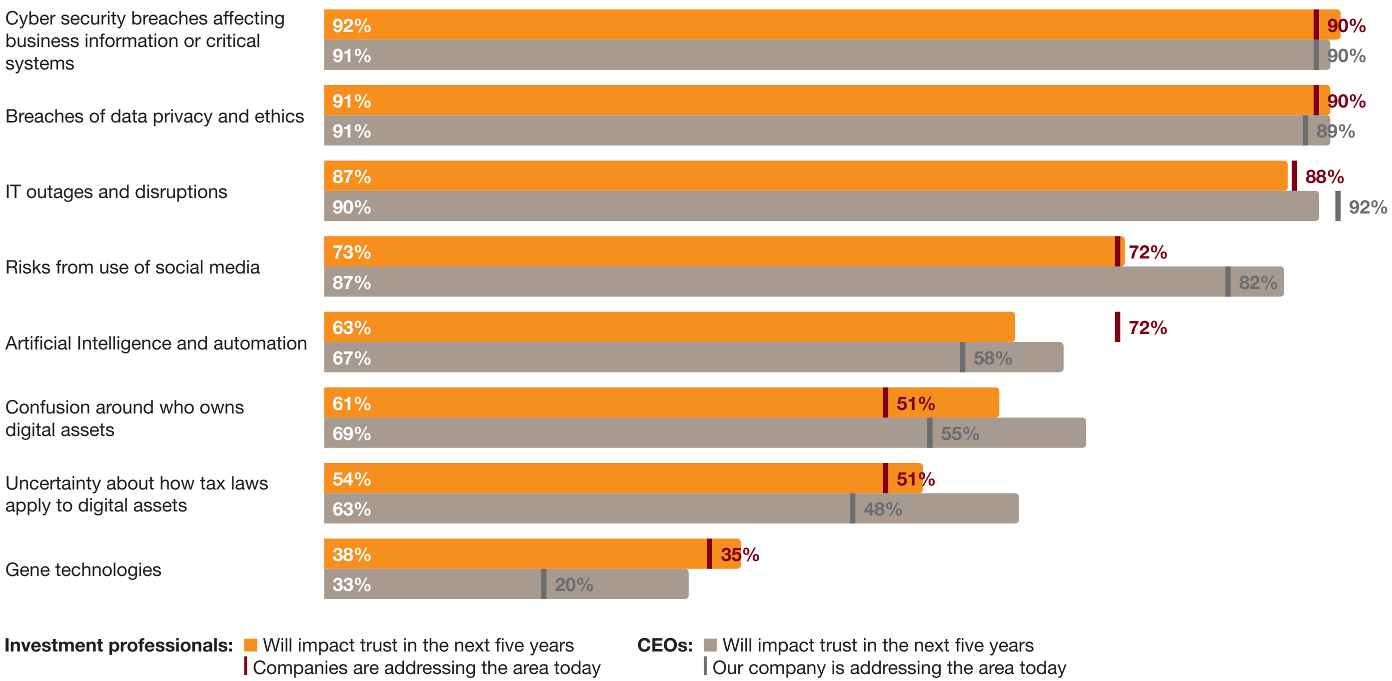
One interviewee highlighted his concern that companies are being told to find purpose in what they do even when it is not linked to the business. "Companies should not have these objectives," he said. "It is often a PR effort to manage public opinion. Some CEOs are convinced that they're doing something for mankind with the business they actually do. They're not doing other things to prove it. The idea of companies doing their job but also doing something that's bettering the world for other reasons is too much."

Another interviewee is concerned that company purpose is becoming less important in an era in which index investing is becoming more widespread. As he explained: "If people genuinely care about purpose, they need to understand what companies are doing, their culture. The only way to have influence is to invest actively."

Figure 12: Investment professionals think that the top three threats to trust are likely to be cyber security and data privacy breaches and IT disruptions

Q: To what extent do you think the following areas will impact negatively on stakeholder trust levels in the next five years?
Q: To what extent are companies addressing the following areas today?

% of respondents answering either to some extent or to a large extent



Technology strikes again

Investment professionals and CEOs both see cyber security breaches, data privacy breaches and IT outages and disruptions as having the most negative effect on levels of stakeholder trust. One interviewee told us, “Cyber security is a key risk and trust is intrinsically linked to cyber security.”

Risks arising from social media are ranked fourth by both groups. As one investment professional said, “Social media means messages are quickly spread around and uncontrollable.” Another shares this concern, adding that “social media can drag down a corporate brand very quickly.” CEOs also see this as a potential trust issue, perhaps because they are more often held accountable for their social media posts – encouraged to use the technology, but aware of the speed of any potential backlash if their messages are received badly. Investment professionals do use social media posts to gain insights into the companies they follow, so companies need to manage the associated reputational risk.

Everyone is learning about what technology can do and what to be mindful of. “Given that IT is a really important issue and will grow, the skills at the board level need to grow,” said one interviewee. Another highlighted the need for investors to be asking the right questions of companies: “I think the real questions around IT are what process you have been through, what technology review processes were used to get here, how have you assessed the value of this project and what was the experience of the people you have. I don’t think people in leadership positions really know what the ‘cloud’ is.” Others talked about the need for governance of technology. “How can you trust technology to do the right thing?” asked one interviewee. “How do you know if you can trust an algorithm? And will the algorithm be designed to benefit the company or the customer?” Another said, “A lot of emphasis is now placed on governance, but is there the same for technology and data? I don’t think so.”

These concerns about governance in technology are becoming so widespread that PwC recently published a paper outlining seven principles for the governance of cyber security to enable boards to ‘step-up’ their response to it as an existential risk issue and explain their approach to stakeholders.[13]

“Trust is an emotion, security is a fact. Security (including cyber) is a basic expectation. People try to break into banks the same way burglars break into people’s houses. You don’t expect that it won’t happen sometimes. It doesn’t mean you can’t trust a bank.”

“Social media is a strong force – it can change underlying customer behaviour. It can make that behaviour, which you thought was under your control, outside your control. The frenzy it can generate, the passion it can generate, from political issues to product offerings, is a risk factor for businesses. You just don’t know when the tide may change. It creates several closed loops – one point of view keeps getting amplified.”

“A good company will be aware of the risks involved in not addressing trust.”

Tough questions about maintaining trust in a digital world:

1. Are you communicating how you ensure that technology is used responsibly within your organisation?
2. Given the level of concern about cyber security, do you talk to your stakeholders about how you safeguard data and the protocols you have in place?
3. Given the vast amounts of data available now, are you engaging with your stakeholders about how they think you could help them distinguish the ‘signal’ from the ‘noise’?
4. Do you explain how what you do for society and the environment benefits your business? And do you ask your stakeholders what they think you should focus on?
5. Do you monitor social media outlets to see what people (including your customers and employees) are saying about you?

Looking for more data?

Figure A: Short term confidence is higher for investment professionals than for CEOs

Q: Do you believe global economic growth will improve, stay the same, or decline over the next 12 months?

% of respondents answering will improve

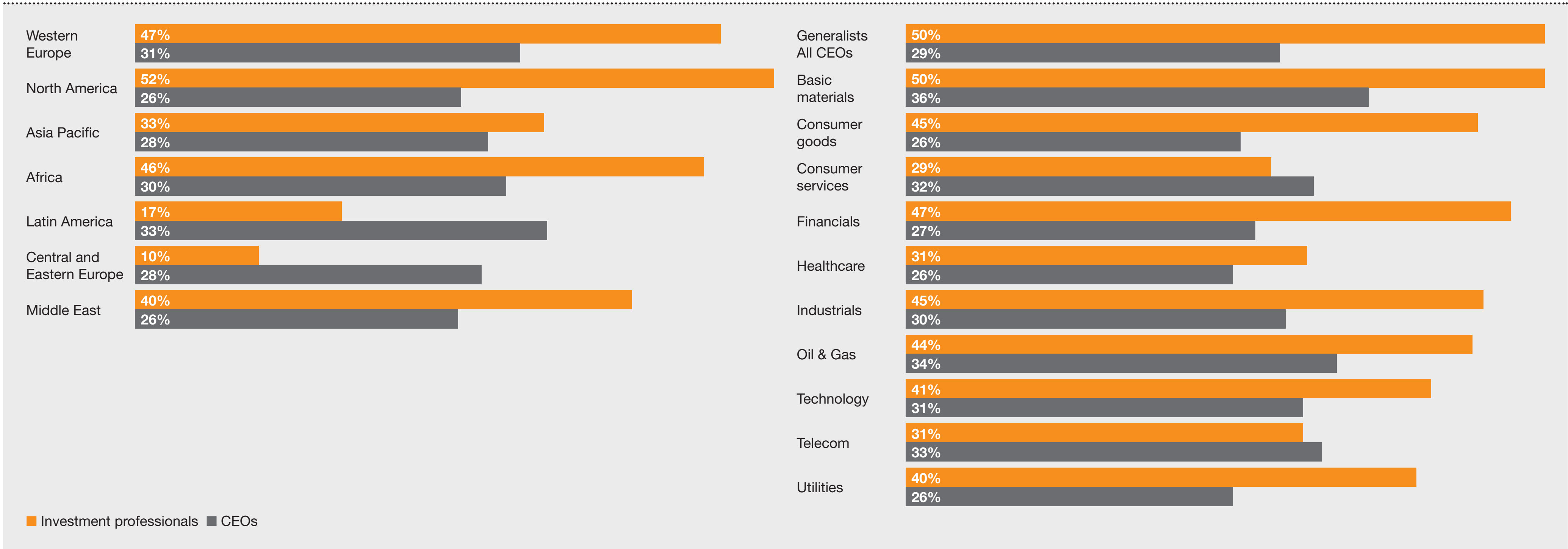


Figure B: Investment professionals are less optimistic about short-term revenue growth than CEOs

Q: How confident are you about the prospects for company revenue growth over the next 12 months?

% of respondents answering somewhat confident or very confident

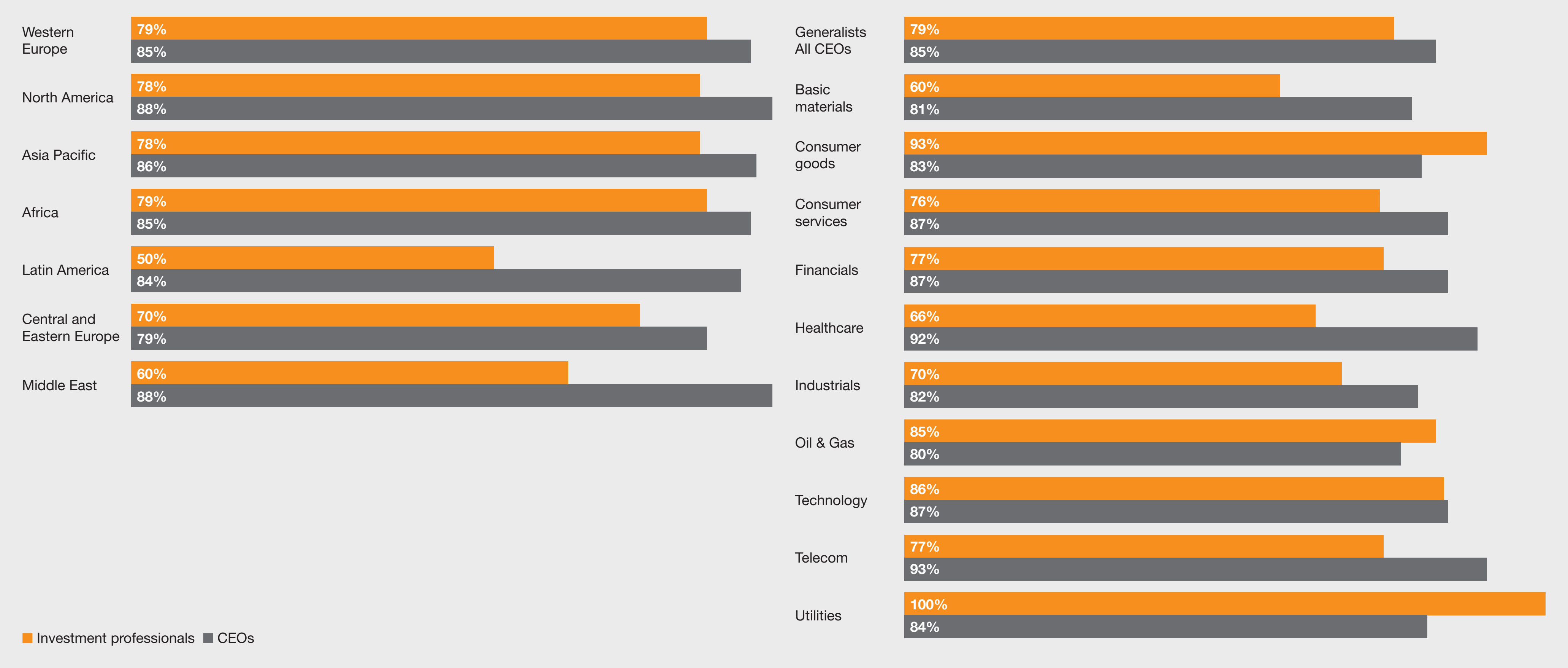


Figure C: Investment professionals are less optimistic about medium-term revenue growth than CEOs

Q: How confident are you about the prospects for company revenue growth over the next three years?

% of respondents answering somewhat confident or very confident

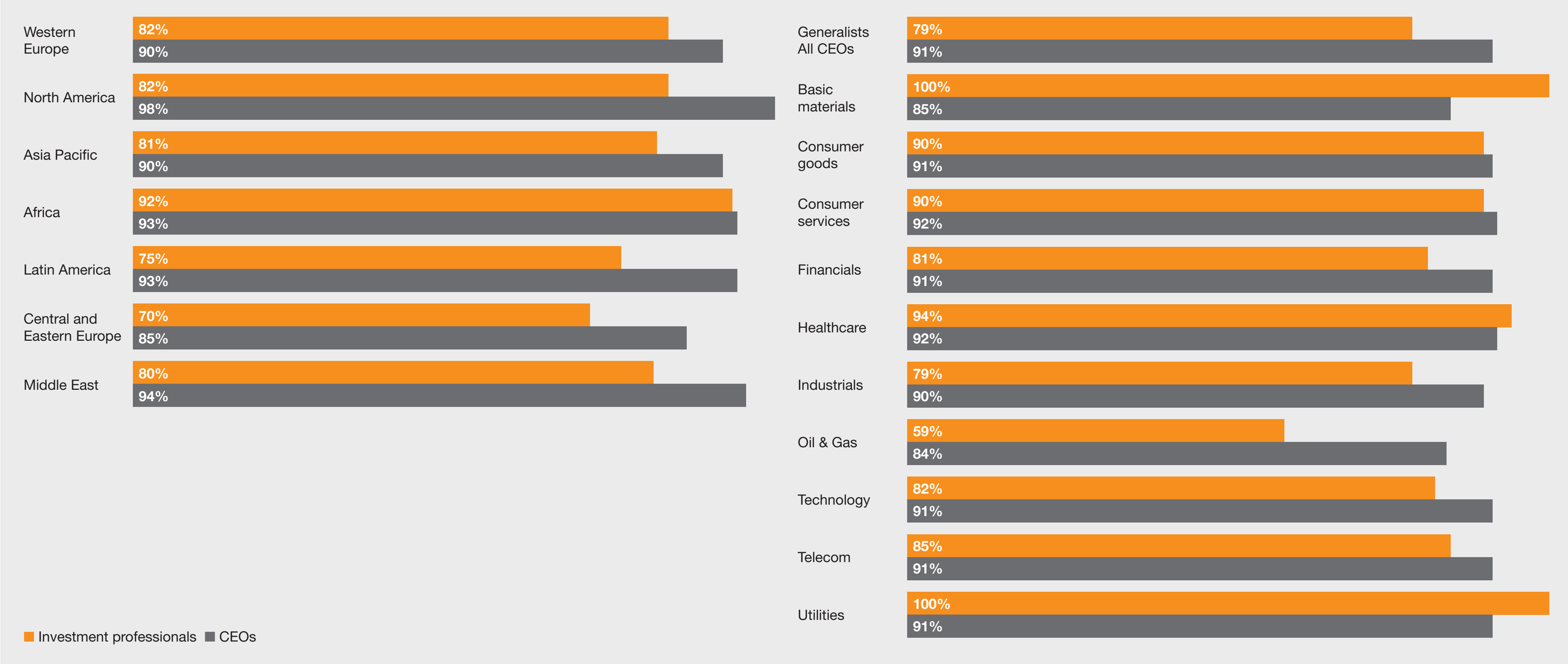


Figure D: Geopolitical uncertainty remains the top threat according to investment professionals

Q: How concerned are you about potential economic, policy, social, environmental and business threats to company growth prospects?

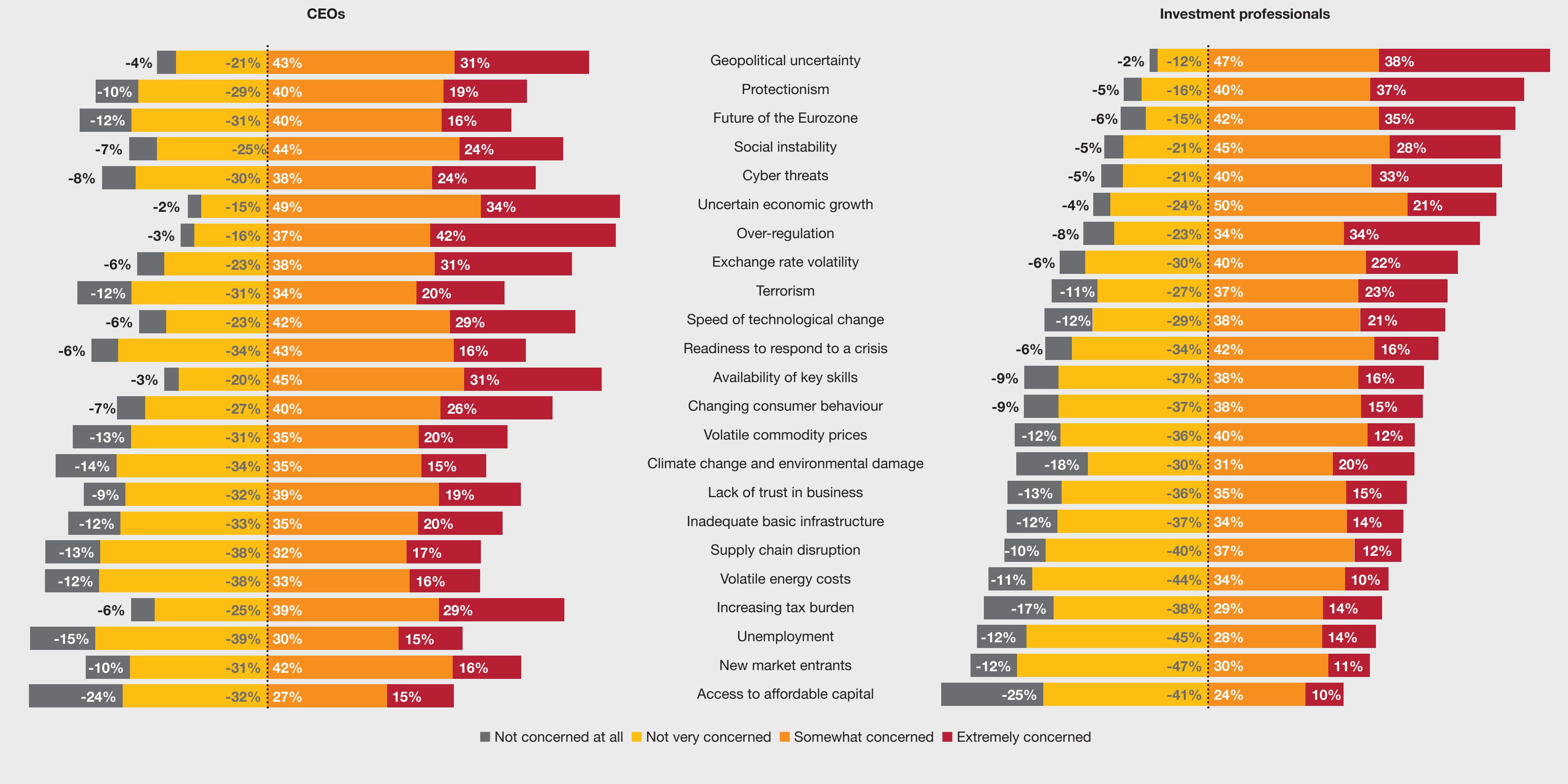


Figure E: Investment professionals see New York and London as the most important cities for growth

Q: Which three cities do you consider most important for the overall growth prospects for the companies you invest in or follow over the next 12 months?

% of respondents naming this city in their top three

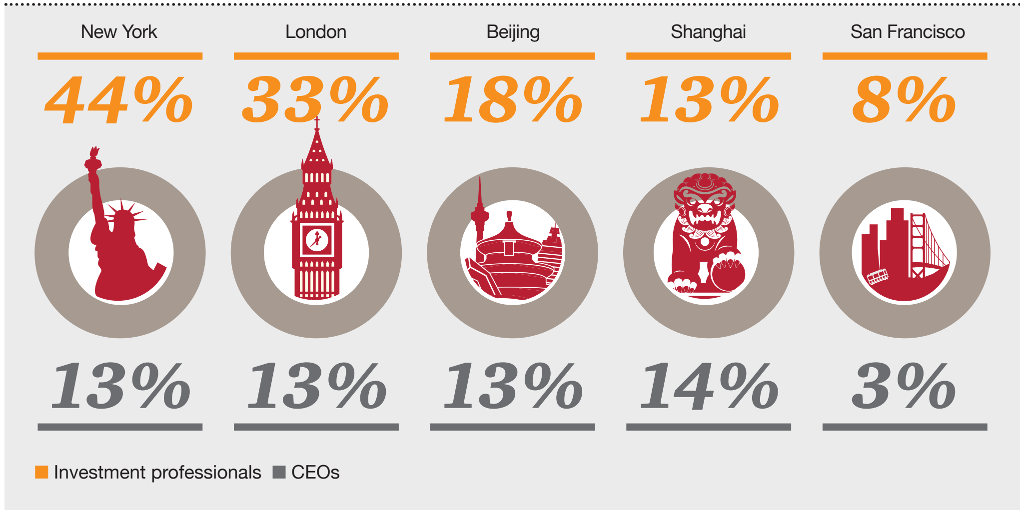


Figure F: Investment professionals see benefits and downsides to globalisation

Q: In your view, to what extent has globalisation helped with the following areas?

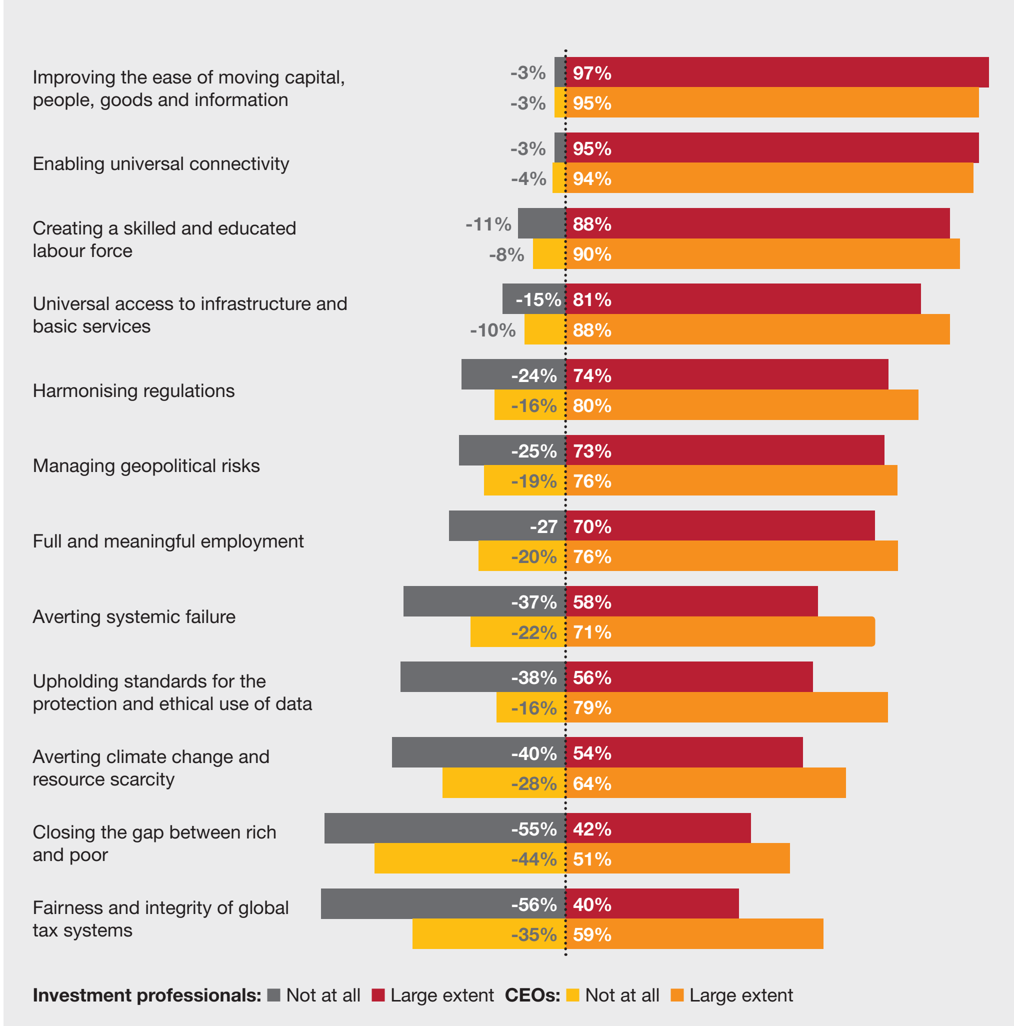
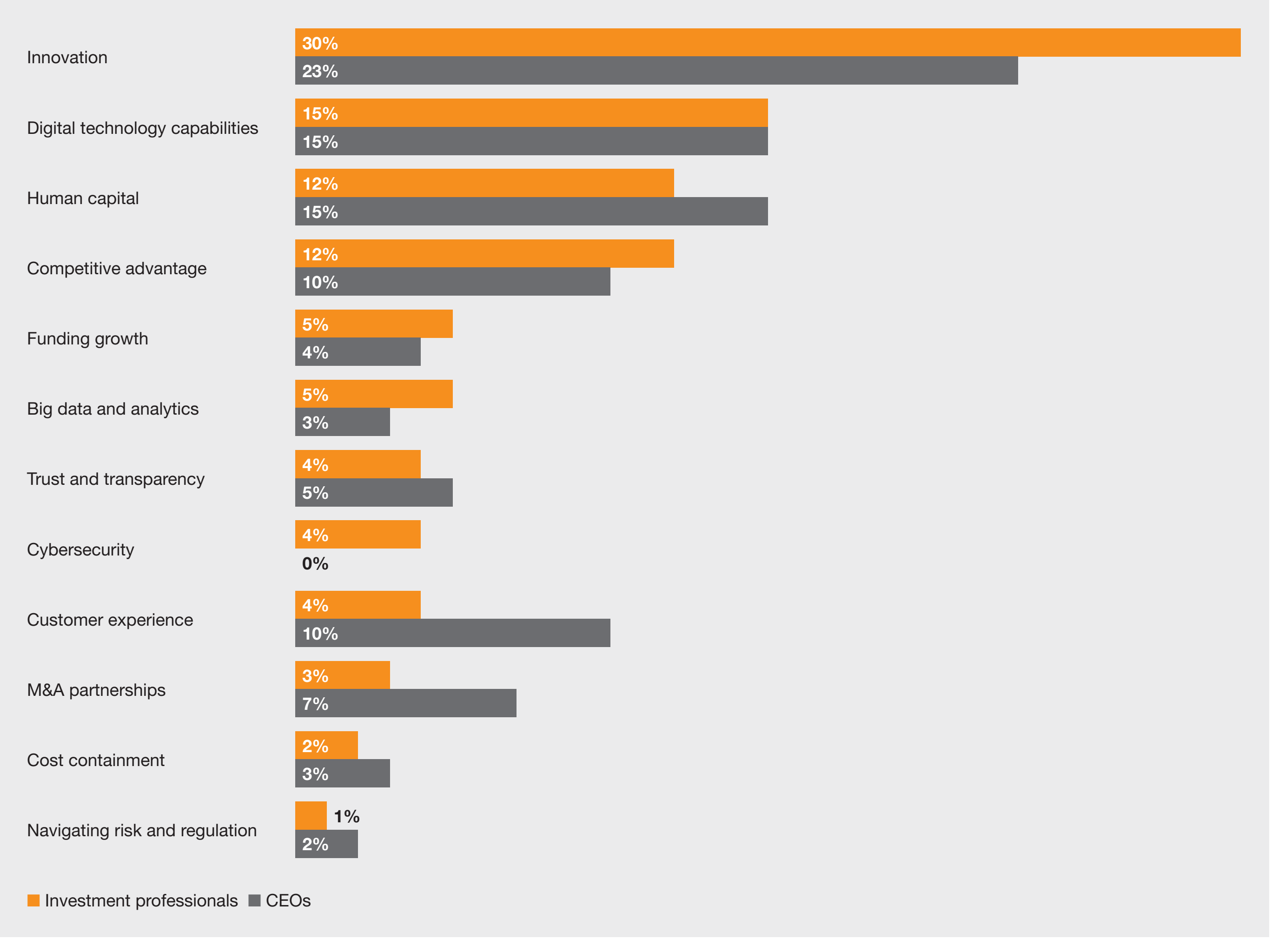


Figure G: Investment professionals prioritise innovation to capitalise on opportunities

Q: Given the current business environment, which one of the following do you think companies should strengthen in order to capitalise on new opportunities?



Research methodology and contacts

We obtained feedback from 554 investment professionals who responded to an online survey running from 17 November 2016 to 16 December 2016. We also conducted in-depth interviews with 38 individuals from a range of regions between November 2016 and January 2017.

Investment professionals answered our questions in relation to the companies they invest in or follow, while CEOs responded in the context of their own organisations.

Figure H: Role

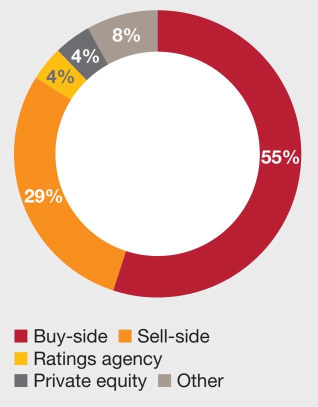


Figure I: Specialism

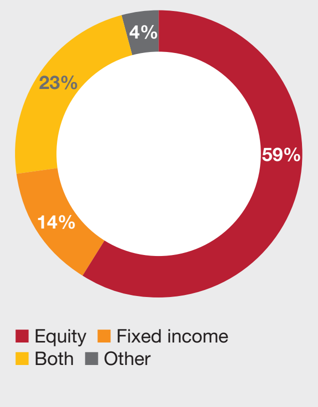
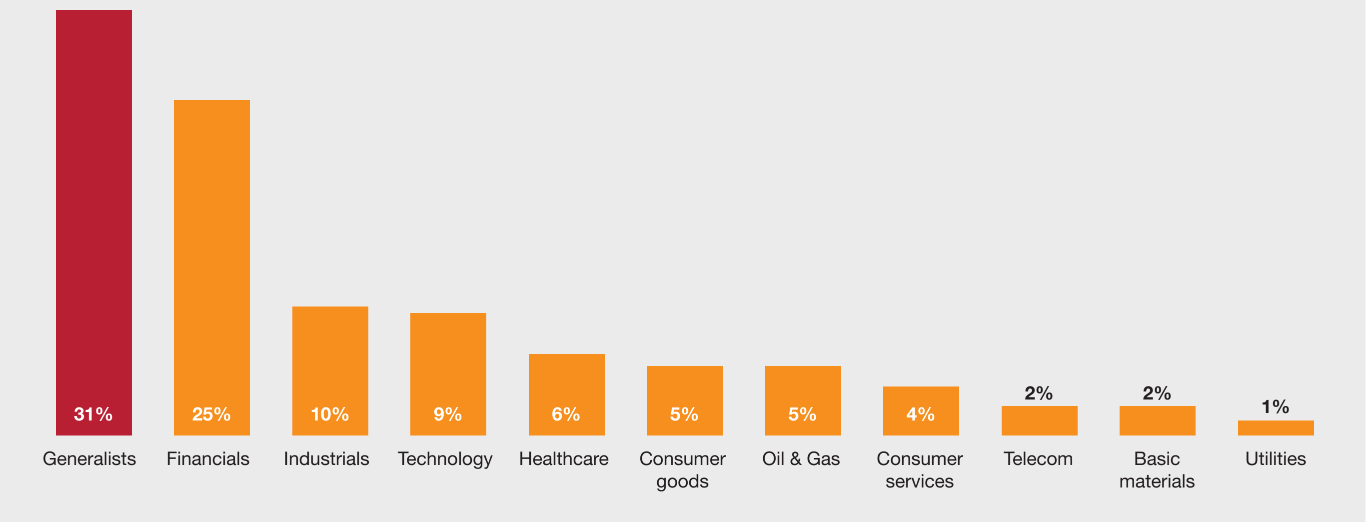
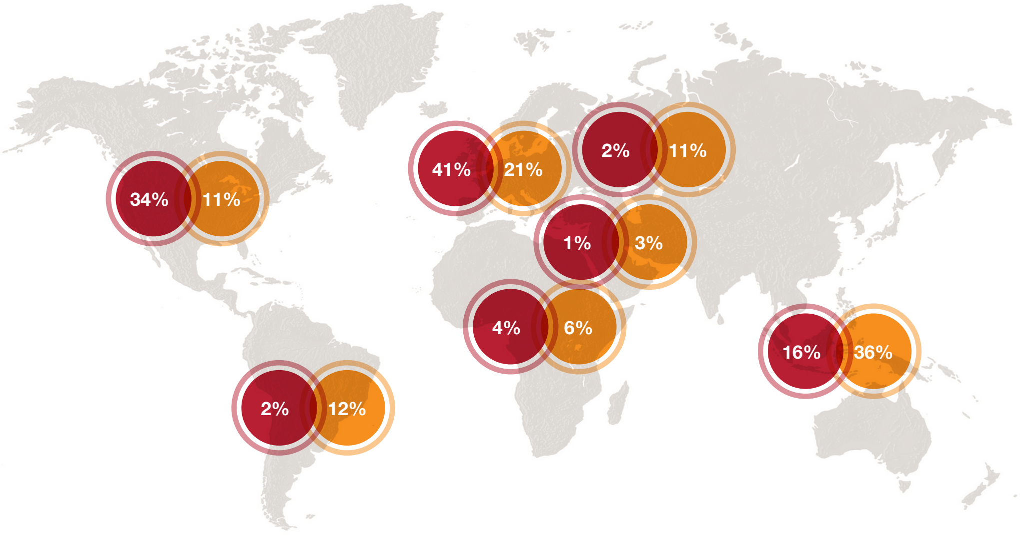


Figure J: Main industry covered



For our 20th CEO Survey, we conducted 1,379 interviews with CEOs in 79 countries. Our sample is weighted by national GDP, to ensure CEOs' views are fairly represented across all major countries. The interviews were also spread across a range of industries. Further details, by region and industry, are available on request.



■ % for investment professionals in each region ■ % for CEOs in each region

Notes:

- Not all figures add up to 100% due to rounding of percentages and exclusion of 'neither agree nor disagree', 'don't know' and 'not applicable' responses.
- The base for figures is 554 investment professionals and 1,379 CEOs unless otherwise stated.
- 57% of the CEOs we surveyed head private companies, while the investment professionals mainly focus on publicly listed companies (though some invest in private equity). Private companies may have private equity investors or listed debt investors, or they may plan to list in the future. Therefore, the views of these CEOs are also of interest when comparing the outlooks of business leaders with those of members of the investment community.
- Where we have included a geographic breakdown, the analysis is based on the base location of the investment professionals and CEOs surveyed.

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