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Opportunity begins at home

Favourable local market steers CEO confidence

14th Annual Global CEO Survey

2nd South African edition

pwc

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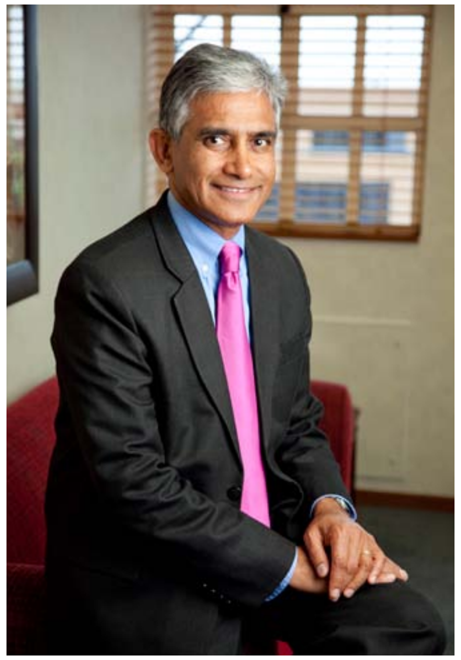


What future are CEOs preparing for? And what steps are they taking to get there?

The 14th Annual Global CEO Survey builds on last year's theme, 'Setting a smarter course for growth', to capture CEOs' shifting attitudes towards operating in a global economy and the actions they are taking to pursue new avenues of growth and opportunity.

As world economies bounce back from the recession that began in 2008, it is evident that the recovery is happening more quickly in some regions and that the balance of economic power is shifting from the developed world to fast-growing emerging economies.

"I thank all those who gave up their valuable time to be interviewed and appreciate the contribution you have made to what is PwC's largest and most in-depth global survey."

About the survey

A total of 1201 CEOs in 69 countries took part in this annual global survey, which was conducted during the last quarter of 2010. This report focuses on South Africa and draws from interviews with 32 local CEOs. It specifically seeks to shed light on the parallels and contrasts in findings here compared to those in other regions and in our previous report, published in January 2010.

The survey set out to examine:

- Whether changes in patterns of globalisation have created new strategic opportunities and/or blocked others;
- What changes to customer behaviour CEOs are preparing for;
- Where innovation will come from in products, processes or technologies;
- How CEOs are addressing newly-emerging operational opportunities and tackling operational constraints in the same areas;
- What specific steps CEOs are taking to address risks that could have strategic business significance; and
- In what ways government influence on the market environment supports or detracts from CEOs' strategic decision-making and corporate competitiveness.

What emerged was a diverging picture of opportunities and threats across the globe, unified by three focal points for change:

- Putting customers at the centre of innovation;
- Bridging the skills gap; and
- Achieving shared priorities with government.

Not one of the crowd

In many ways South Africa finds itself in a unique position. Though the average growth rate lags that of its emerging market peers, it is well ahead of many better-developed economies. At the same time, fiscal discipline and stability in the banking sector have enabled the economy to hold firm while others have stumbled. In this context, it should come as no surprise to learn that South African CEOs remain extremely positive about future prospects, while being acutely aware of the challenges that they and society-at-large face.

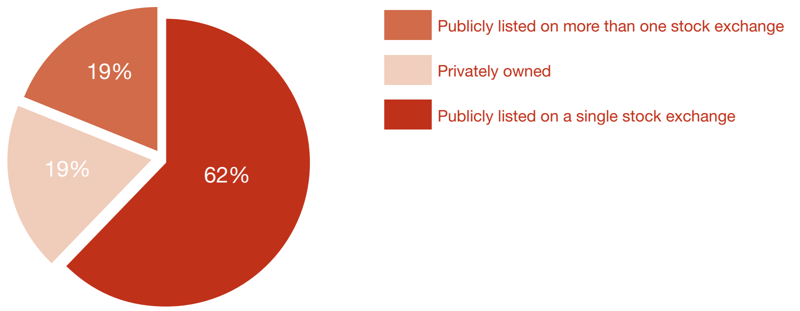
I'm confident you will find the pages that follow filled with valuable information and insights.

Suresh Kana

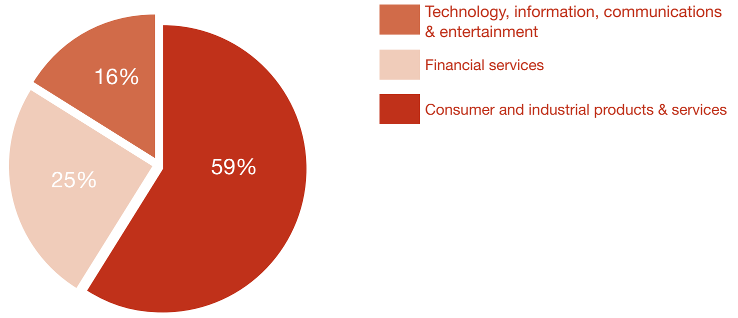
Suresh Kana
Chief Executive Officer
PwC Southern Africa

Participant profile

Interviewees by ownership model



Interviewees by industry sector



Note: Due to the rounding off of percentages and exclusion of 'neither/nor' and 'don't know' responses, not all figures in this report add up to 100%

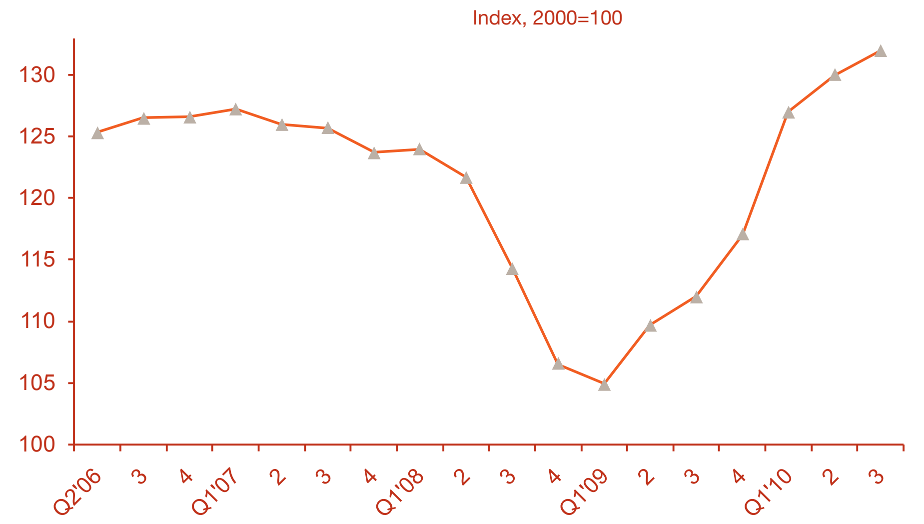
Introduction

The economic context

The global economic recovery that took hold during 2010 saw global gross domestic product (GDP) return to positive territory for the first time since 2007. The South African economy broadly followed the trend of most of its key trading partners by returning to positive real GDP growth during the third quarter of 2009. Since then, it has been sustained at an average level of close to 3%.

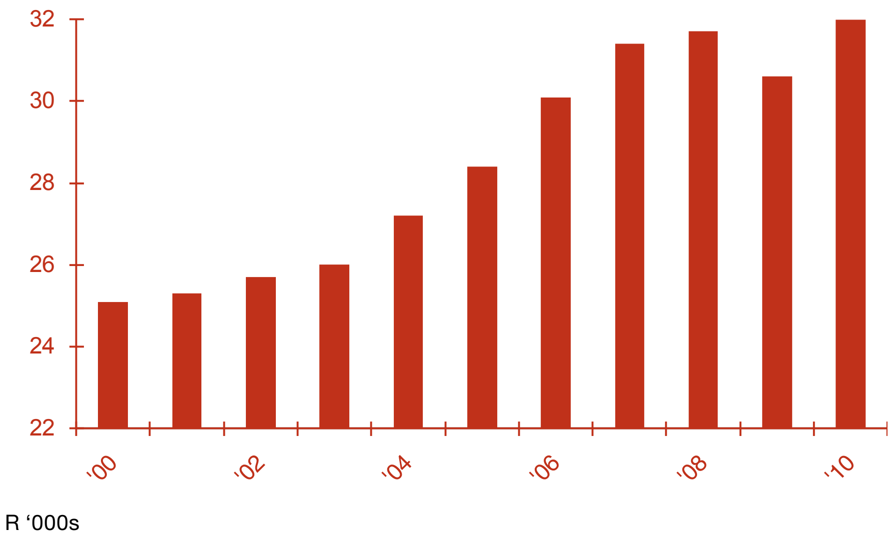
Although the South African economy is not growing as fast as that of India (8.9%) or China (9.6%), economic recovery is firmly entrenched and is also becoming more broad-based, with every key sector of economic activity recording positive real annualised GDP growth in the third quarter of 2010. Although the banking sector has taken longer to recover, credit extension started a firm and broad-based recovery during the second quarter of 2010.

South Africa's business cycle



Prospects for a swift return to the pre-recession economic growth trajectory of above 4% have been buoyed by a resurgence of the country's leading (composite) business cycle indicator, which has risen by more than 25% over the past six quarters, as well as a return to healthy real growth rates for household disposable incomes.

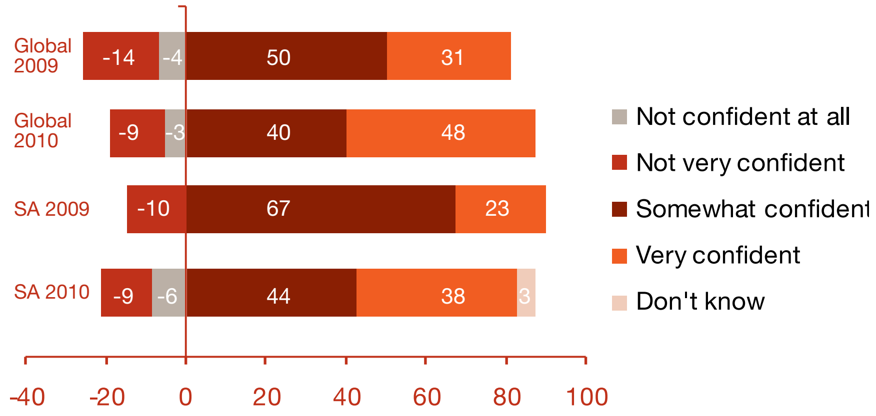
Real disposable income** per capita **of households (at constant 2010 prices)



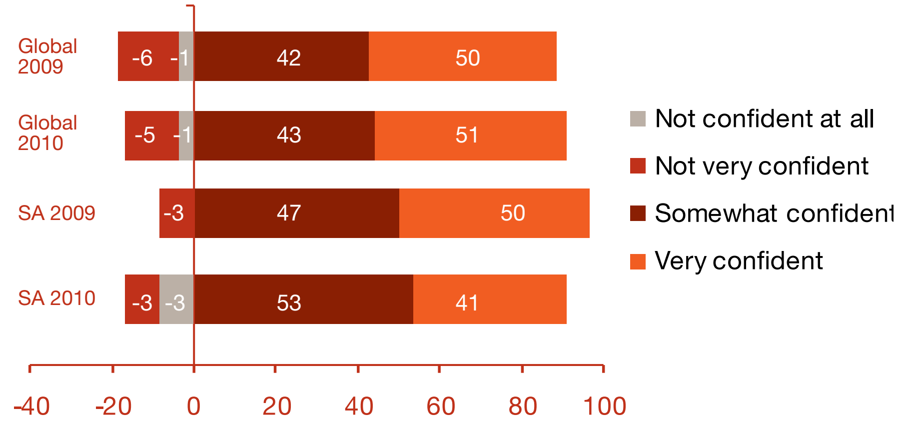
Looking forward

In our last report, no less than 90% of respondents said they were confident about their companies' prospects for revenue growth over the next twelve months, rising to 97% over a three-year forecast period. Following the economic challenges of 2008 and 2009, when it seemed that things couldn't get worse, such optimism was perhaps to be expected. So it's not surprising that such an overwhelming level of confidence has moderated slightly to 82% and 94% respectively for the current reporting period. This result closely parallels those recorded in both developed and emerging markets, which are reflected together in the global average in the accompanying graphs.

CEOs are universally confident about their companies' prospects for revenue growth over the next 12 months

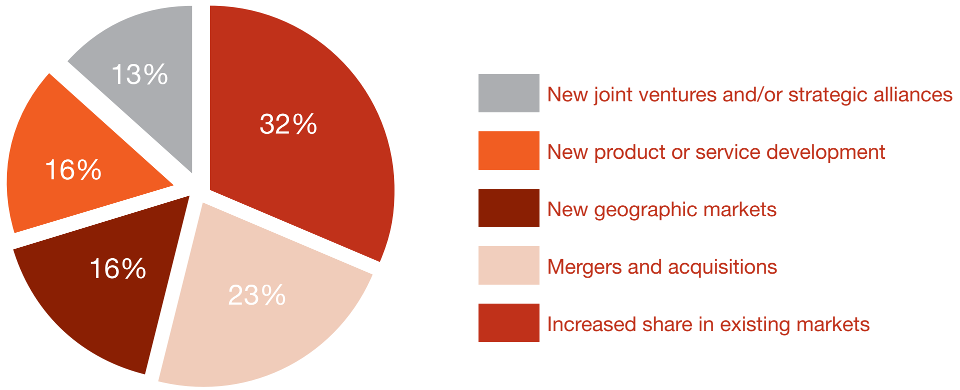


The outlook over the next three years is even more positive



With the external environment affecting the growth strategies of CEOs, many have turned to 'sure bets' like increasing share in existing markets and mergers and acquisitions to expand their businesses. Together, more than half of CEOs view these activities as the main opportunities to fuel growth in the next 12 months.

Focus areas for growth in the next 12 months



94% of South African CEOs expect their business in Africa to grow in the next 12 months.

84% believe emerging markets are more important to their companies' future than developed markets, compared to a global average of 58%.

75% of South African CEOs anticipate changing their organisational structure in the near future.

Concern about macro risks

Uncertainties in the external environment, over which individual businesses have no control, pose some of the most daunting challenges to CEOs across the globe.

We asked South African CEOs to tell us how concerned they are, if at all, about a number of factors:

- **Availability of key skills**

  72% of local CEOs are concerned about the skills shortage. This is not a new issue and while the education and employment challenges facing South Africa remain daunting, this result suggests that labour market reform should be viewed as a policy priority by the Government.

- **Over-regulation**

  66% voiced unease about over-regulation, a 10% decrease since 2009 though still significant.

- **Exchange rate volatility**

  65% say they are concerned about exchange rate volatility, down from 77% in 2009, but still an important concern for many. Over the past two years, a weak US dollar has led to a shift in global portfolio investment flows, resulting in concomitant strength of most emerging market currencies. Of particular concern to South African exporters is the fact that the rand has strengthened against most key currencies in both high-income countries and emerging markets. At the time of writing, the rand had strengthened by 43.7% against the US dollar, by 42.2% against the euro and by 30.9% against the British pound since January 2009

- **Economic volatility or uncertainty**

  63% of CEOs are concerned about economic uncertainty, hinting at fears of fragility inherent in many economies, including South Africa's.

- **Energy costs**

  53% say they are worried about energy costs, down from 70% in the previous year. With the National Energy Regulator announcing in February 2010 tariff increases of 24.8%, 25.8% and 25.4% over the next three years, many electricity users have already swallowed the bitter pill of soaring electricity prices.

- **Lack of stability in capital markets**

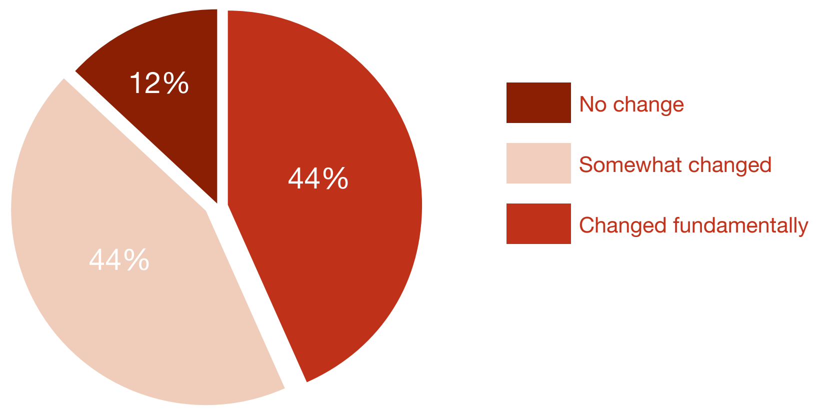
  47% are worried about a perceived lack of stability in capital markets. Of these, 16% said they were 'extremely concerned' about this issue, up from just 3% a year ago.

- **Inadequacy of basic infrastructure**
  40% are concerned about infrastructure, a decrease of 23% from the previous year and perhaps testament to the Government's commitment to infrastructure development, both leading up to and following the 2010 FIFA World Cup.
- **Government responses to fiscal deficit and debt burden**
  34% of South African respondents say they are concerned about government debt, but globally this figure is almost double at 61%. This result is a feather in the cap for South Africa's National Treasury, which had succeeded in generating a fiscal budget surplus prior to the recession and recently lowered its estimation of a manageable budget deficit over the next three years. South Africa's budget deficit remains low by international standards and it seems clear that a lack of taxation revenue growth will not act as an impediment to infrastructure development over the medium term.
- **Protectionism**
  32% of respondents in this survey are concerned about the protectionist tendencies of national governments, a decrease from 50% in the previous year.
- **Inability to finance growth**
  31% have some concern about their companies' ability to finance growth. This figure echoes the views of CEOs globally and is similar to the level recorded in our last report – despite the fact that we now have the lowest interest rates in 37 years and there has been a modest reduction in lending criteria by local banks over the past 12 months.
- **Changes in consumer spending and behaviour**
  28% of CEOs show some concern about changing consumer patterns, compared to just less than 50% in both emerging and developed markets. Only time will tell whether South African consumers are the late adopters some may perceive them to be.
- **New market entrants**
  25% of CEOs are concerned about the threat of new market entrants into their industries, compared to 45% in other emerging markets. Such a distinct contrast could point to significant real or imagined barriers to entry within the South African economy that inhibit competition.
- **Increasing tax burden**
  25% of CEOs are concerned about taxes, which is both a dramatic reduction from the 63% who shared this concern in our last report and significantly less than the 55% global average.
- **Inflation**
  12% say they are concerned about inflation, compared to 30% globally. This figure is down two-thirds from 36% in 2009 and reflects the success of the South African Reserve Bank in reducing the consumer price index (CPI) from 8.6% in February 2009 to 3.6% in November 2010.

Meeting the challenge of change

The economic realities of the past few years have forced CEOs to not only change the way they think, but also how they run their businesses.

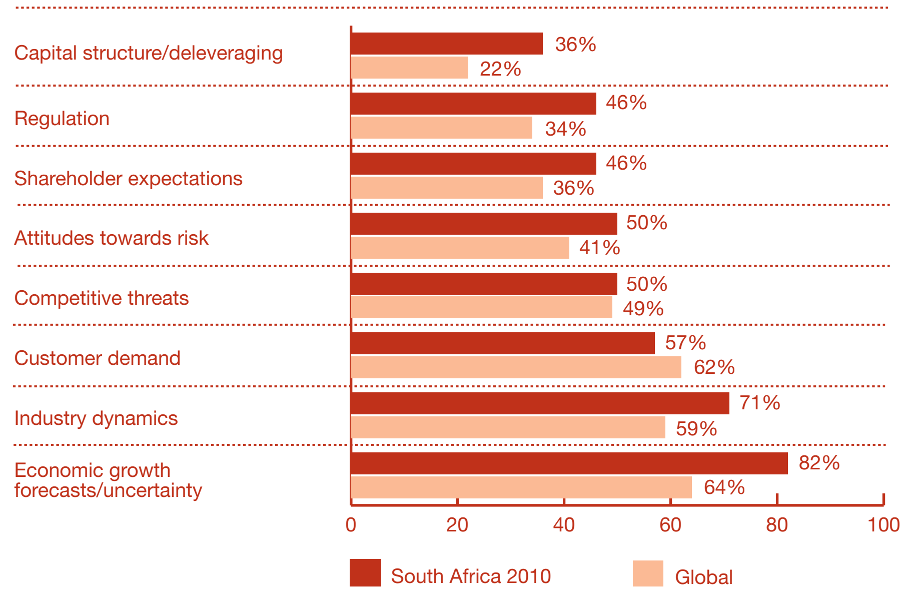
Most companies have changed their strategies over the past two years



88% say their companies' strategy has changed 'somewhat' or 'fundamentally' in the past two years.

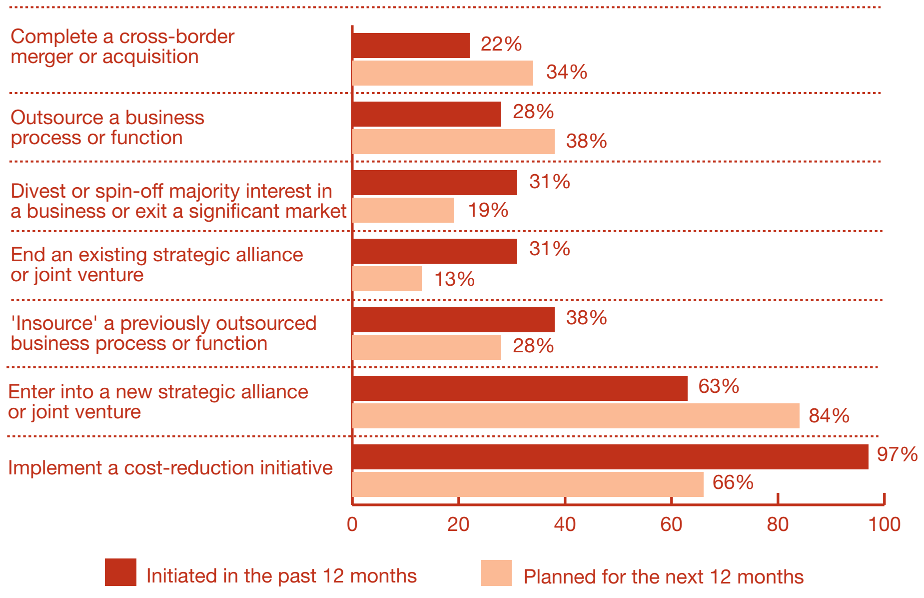
94% anticipate 'some' or 'major' changes in their approach to managing risk in the near future.

Change has been driven by a number of factors



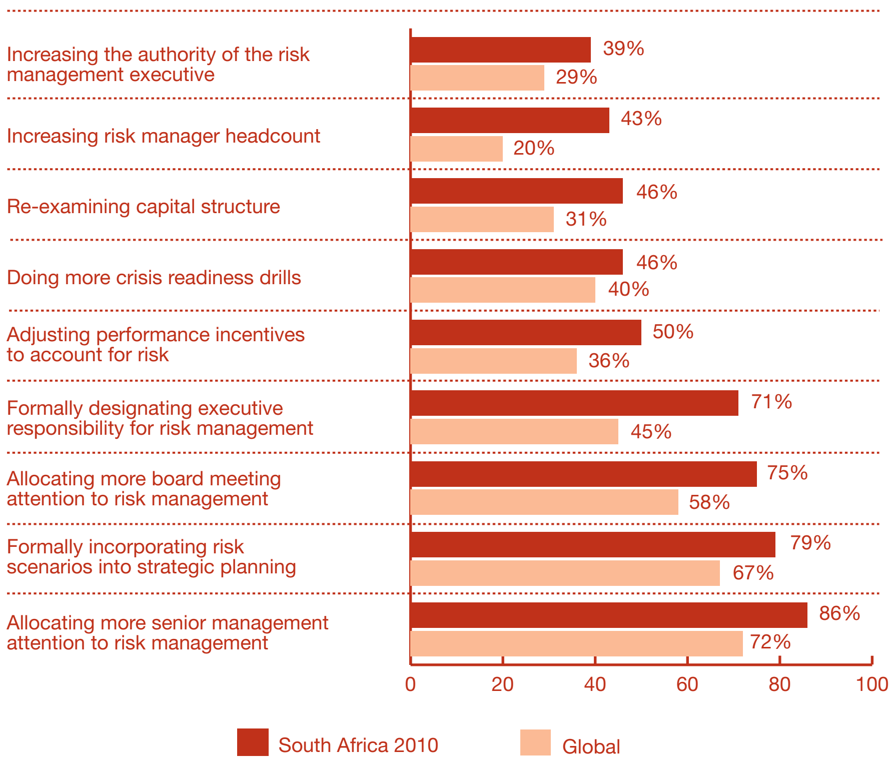
Driven by anxieties about industry dynamics and economic uncertainty, restructuring has led a range of activities undertaken by companies to adapt to the operating environment they currently find themselves in.

Restructuring activities initiated during the past 12 months and planned for the next 12 months



With change comes risk and this has had a decisive impact on the level of attention given to risk management at every level within organisations.

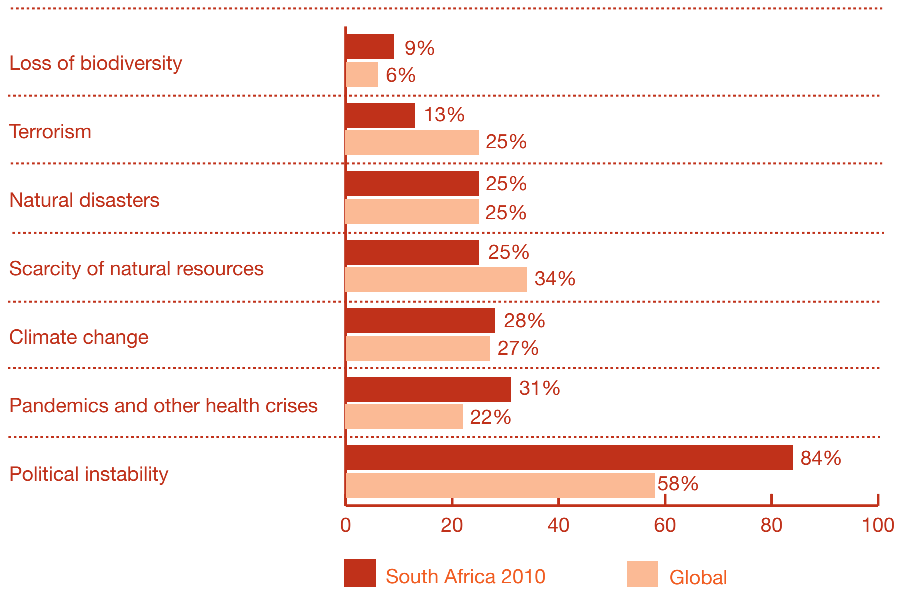
Companies are taking a range of steps to improve the management of risk that accompanies a change in strategy



It is worth noting that South African companies appear to be leading their global peers in taking proactive steps to manage risk.

Confronting global risk

Volcanic eruptions, earthquakes, floods, landslides, fires and drought have devastated vast areas of the world in the last year and are a humbling reminder of the powerful factors that remain beyond human control. Meanwhile, fear of terrorism and political instability remain significant concerns globally.

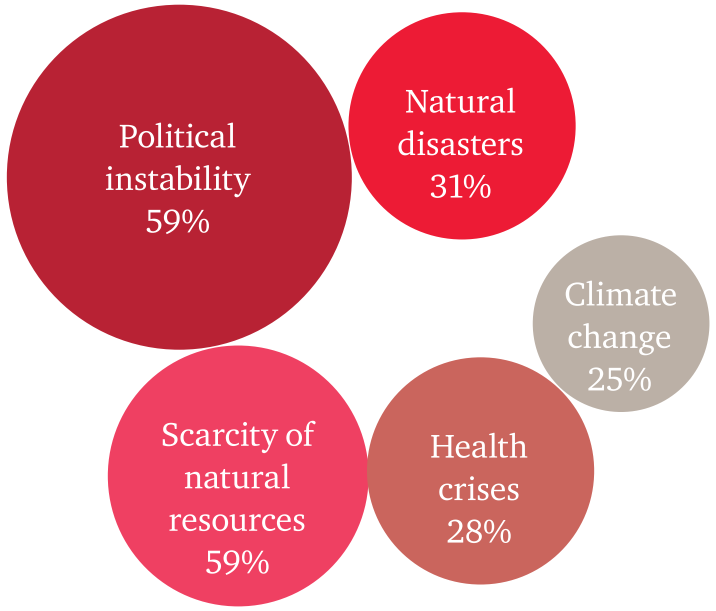


CEOs are most concerned that their companies' growth prospects could be undermined by a number of global risks in the next three years

South African CEOs say they are most concerned about the potential impact of public policy on their businesses, an anxiety that is far greater locally than globally. This uncertainty may be fuelled by disagreements on policy amid ongoing public debate around issues such as the nationalisation of mines and labour reform.

Being concerned about risk is one thing, but explicitly factoring it into strategic planning and risk management activities is an area where local CEOs are performing better than their global counterparts.

Top five global risks factored explicitly into strategic planning and risk management programmes by South African CEOs



Bridging the skills gap

Creating new jobs and skilling the workforce with the necessary know-how is a political, social and business imperative and one that South African CEOs are taking seriously.

South Africa faces the twin dilemmas of high unemployment and a shortage of skills. More than four million South Africans are unemployed and the recession further exacerbated the shortage of jobs in the economy with the unemployment rate climbing to 25,3% in the third quarter of 2010.

90% of South African CEOs say their companies will increase their commitment to creating and fostering a skilled workforce over the next three years. This percentage is almost 10% higher than the global average.

94% say they will increase their commitment to maintaining the health of their workforce, compared to 71% globally.

75% will increase their commitment to reducing poverty and inequality in the country, compared to 42% globally. Of course some countries need to do more in this area than others and it is perhaps worth bearing in mind that the United Nations Human Development Agency rates South Africa as one of the most unequal countries in the world, alongside the likes of Colombia, Haiti and the Central African Republic.

Talent management

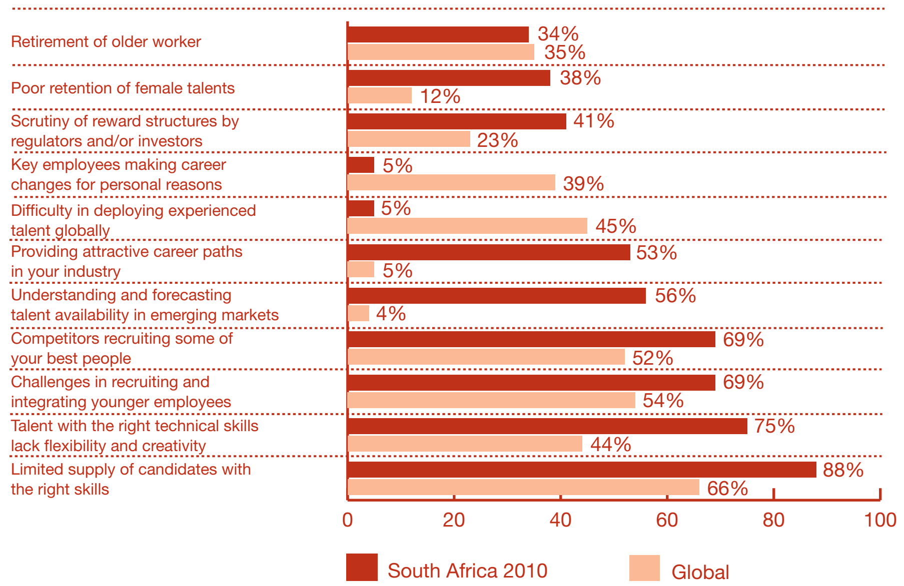
Attracting, recruiting, integrating, developing and retaining employees to meet current and future business objectives can be extremely frustrating in the South African context. Despite the prevailing difficulties, CEOs are optimistic.

91% of CEOs anticipated making either some or major changes to their strategies for managing talent.

72% said that headcount in their organisations stayed the same or increased over the past 12 months. While this compares favourably with the global average of 64%, 25% of local CEOs also reported that they had reduced staff numbers by 5% or more.

38% expect their headcount to increase over the next 12 months.

Considering the talent required for the success of their businesses over the next three years, CEOs expect to face a number of challenges



As the accompanying graph demonstrates, the scale of the problem posed by the scarcity of talent in South Africa can be seen in the contrast between local and global results for almost every variable surveyed.

On the positive front, South African CEOs say they are taking remedial action:

72% aim to work more closely with government and educational institutions to improve skills in the talent pool.

72% intend to use more non-financial rewards to motivate staff.

66% plan to change their talent strategy to attract and retain more women.

56% say their companies plan to set compensation limits for top executives, compared to 40% globally.

50% wish to incentivise workers under 30 differently to other employees.

Putting customers at the centre of innovation

As markets mature, so there is a growing need for new products and services to drive growth. This is leading to an increasingly customer-centric wave of innovation, which not only promises customers a better product experience, but also an opportunity for companies to differentiate themselves from competitors and increase revenue. These dynamics apply both in the business-to-business and consumer markets.

Of respondents for whom consumers represent more than 33% of revenues:

94% are adjusting their strategies to accommodate consumers' increasing use of mobile devices and social media to voice their needs and preferences to companies.

86% intend to improve their environmental and corporate responsibility practices as these become increasingly influential in consumers' purchasing decisions.

85% aim to change their strategy in the next three years to address consumers' priorities regarding price and value for money.

79% plan to adjust their business strategies to allow consumers to play a more active role in product and service development.

Of all South African CEOs surveyed:

66% believe it is important to develop products that are environmentally friendly.

16% expect government assistance, including financing, tax credits and/or technology transfer, to boost their innovation initiatives.

Protecting consumers

With the imminent introduction of the Consumer Protection Act in South Africa, the importance of taking action to protect consumers' interests is high on the agenda:

85% of CEOs plan to increase their commitment to protecting consumers' interests over the next three years.

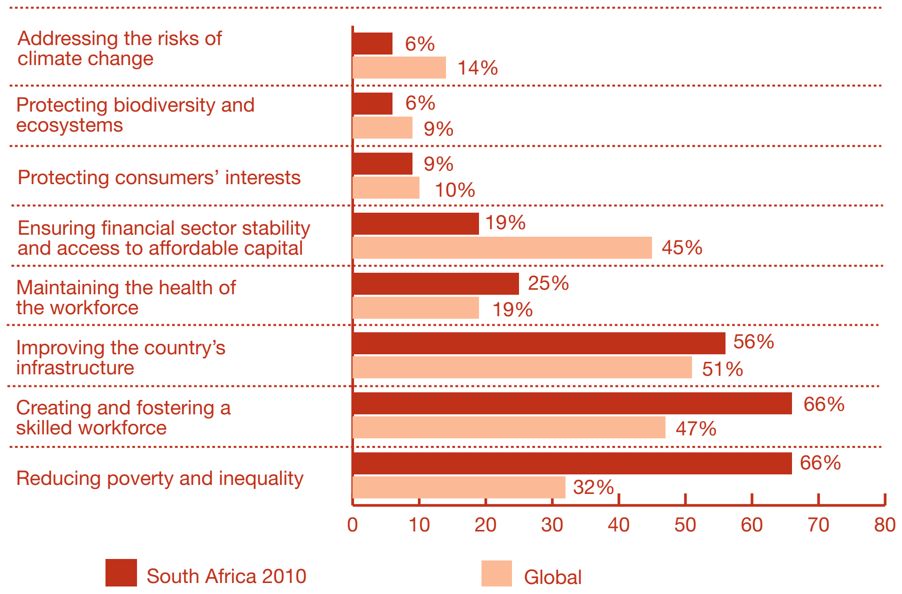
72% anticipate changing the way in which they manage their corporate reputation and build trust with stakeholders.

Achieving shared priorities with broader society and government

South African CEOs are cognisant of the responsibilities they and their companies have in society. They also have high expectations about the role government should be playing.

Compared to their global counterparts, their concern about the role of government is most pronounced in the areas of reducing poverty and inequality and creating a skilled workforce. On the other hand, they are far more upbeat than their global peers about the state of the financial sector and their ability to access affordable capital, no doubt a reflection of the fundamental soundness of this aspect of the economy.

Issues CEOs think should be government priorities



91% of South Africa CEOs believe business will actively support new government policies that promote growth that is financially, socially and environmentally sustainable at global, national and local levels.

72% consider that a partnership between government and business will be more effective at mitigating key global risks like climate change, terrorism and financial crises.

Conclusion

It is encouraging to note an overall positive outlook from CEOs. Although the recovery may sometimes be slow or 'fragile', CEOs are gearing up for better times ahead.

Over the past 14 years, the PwC Annual Global CEO Survey has given business leaders, governments and the world's business community a unique insight into the perspectives, vision and decisions of CEOs across the world. The report is the result of extensive research consisting of both a quantitative survey and in-depth interviews. This, the second South African edition, is being released simultaneously with the global edition at the Annual Meeting of the World Economic Forum in Davos, Switzerland.

Five years ago, few people had heard of subprime mortgages and the economic dynamics of the present would have been inconceivable. Nevertheless, as with our previous report on South Africa, local CEOs consistently demonstrate a high level of optimism about the future that is underpinned by a keen awareness of the opportunities and challenges that lie before them.

In adapting to the altered market conditions, the vast majority have reshaped their business strategies and initiated cost-reduction initiatives. Changing strategy is inherently risky and the survey shows that risk management is being given more attention than ever before at both a strategic and executive level. Pleasingly, South African businesses appear to be more proactive than their global peers in taking action in this area.

While many businesses based in developed nations scramble to find growth opportunities in far-off emerging markets, South African CEOs recognise that the greatest opportunities are to be found at home. Most are taking action to become better corporate citizens and offer their customers greater interaction and value as these factors become increasingly influential in consumers' purchasing decisions.

While remaining positive in their outlook, South African CEOs aren't naive about potential pitfalls. The skills shortage, worries about over-regulation and exchange rate volatility coupled with policy uncertainty top the list of their concerns.

But, CEOs also recognise the role that business has to play in developing the nation. No less than 90% say their companies are increasing their commitment to creating and fostering a skilled workforce as well as changing their strategies for managing talent. Three-quarters also say they will increase their commitment to reducing poverty and inequality over the next three years.

Such undertakings suggest that CEOs are taking a view that considers the long-term sustainability of their businesses, which requires renegotiation of the balance between corporate profitability and social well-being. Future reports will track these developments.

Finally, it is encouraging to note an overall positive outlook from CEOs. Although the recovery may sometimes be slow or 'fragile', CEOs are gearing up for better times ahead.

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